M (PVT) LTD
versus
THE COMMISSIONER GENERAL, ZIMRA

SPECIAL COURT FOR INCOME TAX APPEALS
KUDYA J
HARARE, 24 November 2014 and 30 July 2015

INCOME TAX APPEAL

F. Girach, for the appellant
T. Magwaliba, for the respondent

KUDYA J: This appeal was initially filed in the normal way. It commenced by way of notice of appeal filed on 13 June 2012 and was followed by the appellant's 10 page case inclusive of 4 annexures on 7 September 2012. Thereafter the Commissioner's 42 page case inclusive of 15 annexures was filed on 8 November 2012. At the pre-trial hearing of 15 September 2014 three issues were identified for determination of the appeal. These were firstly, whether or not a theft occurred, secondly, if so, whether the appellant was entitled to the deduction claimed and lastly whether or not the respondent should have waived the penalty in full.

At the appeal hearing of 24 November 2014 the parties submitted a statement of agreed facts and proceeded to argue on the legal contentions. The appeal thus proceeded by way of a stated case in which the sole issue for determination was couched thus:

> "Where an employer suffers a loss in consequence of a theft of monies which is perpetrated by a person or persons other than a shareholder, or an owner and such theft occasions loss to his business, is that employer entitled to a deduction under s 15 (2) (a) of the Income Tax Act [*Chapter 23:06*]."

The agreed facts were as follows,

1. The appellant is a duly registered company carrying on the business of providing specialist medical services to members of the public and is based in Harare. The respondent is the Commissioner General of the Zimbabwe Revenue Authority whose authority to act on behalf of the Zimbabwe

Government in collecting taxes is authorised by the Zimbabwe Revenue Authority Act [*Chapter 23:20*].

2. On 7 February 2012, the respondent issued an amended assessment for income tax on the appellant for the tax year ended 31 December 2010. A copy of that assessment is annexed here to and marked annexure A of appellant's case and annexure H of respondent's case.
3. Thereafter the respondent issued an amended assessment, the effect of which was to increase the taxable income of the appellant. In addition, the respondent imposed a penalty in the sum of $41 856-65.
4. The appellant then objected to the amended assessment by way of letter 13 February 2012, a copy of which is annexed hereto and marked annexure B of appellant's case and annexure J of respondent's case. The basis for objection being that the theft of the monies by managerial or subordinate non-managerial employees who were not shareholders was an unavoidable inherent risk sustained in the generation of taxable income thatwas deductible. The appellant further objected to the imposition of the 100 per cent penalty as punitive and shocking on the ground that it had fully disclosed the cash discrepancy and did not intend to avoid or postpone the payment of tax.
5. The respondent rejected the objection made by way of letter dated 18 May 2012 but allowed a reduction of the penalty from 100 per cent to 30 per cent. A copy of the letter is annexed hereto and marked Annexure C of appellant's case and annexure L of respondent's case. In the ruling the commissioner did not dispute the discovery of the cash discrepancy in the report of the independent firm of accountants. The report established that the systems administrator and after her the bookkeeper together with the managing director had access to the cash locked in the bag that was in turn locked in the safe. And in addition, the systems administrator, the credit controller and the managing director were the only ones with access to the safe where the lockable bag was kept. The Commissioner ruled that the appellant had failed to exclude managerial employees from the theft. He reduced the penalty from 100 per cent to 30 per cent which entailed a refund of US$ 29 299-66 to the appellant.
6. The appellant then through its legal practitioners noted an appeal by way of letter dated 13 June 2012, a copy of which is annexed hereto and marked

annexure D of appellant's case and annexure M of the respondent's case against the ruling and the failure to remit the penalty in full.

7. It is common cause between the parties that the provision for audit fees in the sum of $42 000 was re-written into income for the following fiscal year and is therefore no longer in issue.
8. It is also common cause between the parties that:
   a. A theft occurred in the sum of $93 459 and that such theft constitutes a loss sustained by the appellant;
   b. Whilst the appellant has been unable to ascertain the identity of the person or persons responsible for such theft, the theft was not perpetrated by a shareholder or any person having a direct interest in the business of the appellant;
   c. Persons having access to monies on a day-to-day basis were a systems administrator and a bookkeeper and there is no direct evidence to implicate these persons;
   d. The appellant engaged the services of an independent firm of accountants to conduct an investigation and the report confirmed the theft of the amount aforesaid, but such investigation could not identify the person or persons responsible for the theft. The report was attached as Annexure B to the respondent's case and is entitled"Factual Findings Report to the Directors on the results from the foreign currency transactions detailed review". The report, amongst other things, established that the appellant was not banking the foreign currency receipts it received but was keeping it in a locked bag which was in turn kept in a locked safe.
9. At the material time, all persons requiring services from the appellant were obliged to pay and did pay for such services in cash. Appellant required patients to pay in cash as the state of the economy then had resulted in medical aid providers experiencing difficulty in meeting claims and claims made on them were frequently not met.
10. Appellant was at that time one of the few providers of such services in the country and thus was particularly busy.
11. The cash was collected and receipted by a cashier who then handed over the cash to her superior from time to time.

12. At all material times, therefore, there was a real risk of the misappropriation of funds occurring given the state of the economy and the dire need for services, the theft suffered was incidental to the carrying on of appellant's business activities and inseparable there from.
13. In the event of the issue set out hereinunder being determined in favour of the appellant, the penalty imposed will be set aside.

The impact of r 11 documents

At the commencement of the appeal hearing both counsel advised the court that it was not necessary for the respondent to file r 11 documents firstly, because the parties were proceeding by way of a stated case and secondly, because these documents were already on record as annexures to their respective cases. A closer reading of r 11 discloses that it is mandatory for the Commissioner to transmit these documents to the Special Court whether the parties proceed by way of stated case or by contested case. Rule 11 documents consist of a certified copy or extract of the assessment made upon the appellant, the notice of objection and the notice of appeal together with related correspondence exchanged between the parties and the copy and reasons for the decision appealed against. The rule 11 documents can only be dispensed with if they form part of the statement of facts. The statement of agreed facts only incorporated a copy of the assessment, the notice of objection and appeal and the decision appealed against. It did not include material correspondence attached to the respondent's case. It is clear to me that the parties intended that the annexures that are attached to the respondent's case should form part of the statement of agreed facts. I will therefore take them as part of the statement of agreed facts in this judgment.

The annexures disclose more detail on the interactions between the parties. On 10 April 2011 the appellant submitted an income tax annual return for the tax year ending 31 December 2010 [annexure C of Commissioner's case] with a tax computation attached together with detailed monthly income and expenditure schedules D and E respectively**.** It claimed deductions of the provision of audit fees in the sum of US$42 000-00 and a cash discrepancy in the sum of US$93 459-00. The return initiated discussions between the parties which culminated in the submission of a second income tax computation in which the provision for audit fees were added back to income. The appellant's tax liability rose from the initial US $37 929-00 to US$ 50 907-00. The appellant had paid the initial tax liability in three quarterly instalments of US $5 038 on 25 March 2010, US$15 711 on 25 June 2010 and

US$17 180 on 20 December 2010.A liability of US$ 12 978-00 remained outstanding on the revised tax return [see annexure F and G of the Commissioner's case]. On receipt of the second income tax submission, the respondent added back to income both the provision of audit fees and the cash discrepancy and assessed the appellant to income tax in the sum of US$79 785-00. It duly deducted US$37 929-00 that had been duly paid leaving a shortfall of US$41 856-65. In addition it imposed penalties in an equivalent amount [annexure A of appellant's case and H of respondent's case]. The appellant paid US$12 978-00 on 28 October 2011 [annexure I dated 30 March 2012] before the amended assessment with had been raised and dispatched. On 30 March 2012 the respondent demanded payment of the outstanding principal of US$28 878-65 together with the full penalty of US$41 856-65 in the aggregate sum of US$70 735-30 [annexure I]. These amounts were duly paid on a without prejudice basis on 4 April 2012 [annexure K1 and K2].

The dilemma

In oral argument, Mr *Girach* for the appellant contended and Mr *Magwaliba* for the respondent conceded that the managing director was not one of the possible defalcators of the cash. I found myself on the horns of a dilemma when I compared the statement of agreed facts and the concession to annexures A and B of the respondent's case. Annexure A captures some enquiry conducted by a legal practitioner presumably on behalf of the appellant to establish how the opening and closing balances in annexure B were reached, how cash payments were recorded and receipted, why in the second period the payments exceeded the cash received and who had access to the safe. They appeared to be in contradiction. The statement of agreed facts and the first sentence of clause 1.2 of the ruling of 18 May 2012 and the first two paragraphs of Mr *Magwaliba's* written heads of argument accept as a fact arising from the report of the independent firm of accountants that there was a cash discrepancy.

The existence of the cash discrepancy depended upon the accuracy of the books of account that were at hand during the verification exercise conducted by the independent firm of accountants. The report established that the systems administrator did not keep a proper record of all the payments she purportedly made on behalf of the appellant. The first issue at the pre-trial hearing referred to trial sought to determine whether in the light of this finding the appellant was a victim of theft. The report of the independent firm of accountants further established an acute failure by the appellant to keep proper books of account for foreign currency transactions between July 2008 and August 2009. Such failure no doubt affected the final product, annexure B.

That this was a difficult mandate is self-evident from clauses 1.5 and 1.6 of the report. In order to make sense out of the available transactional information the appellant and the independent accountants resorted to the use of the International Standard on Related Services (ISRS) 4400-*Engagements to Perform Agreed upon Procedures Regarding Financial Information.* This standard precludes the independent accountants from expressing an assurance on the correctness of their findings. They are denied the right to express an audit opinion on the accounts or other contents of the report. The standard leaves it to “the users of the report to assess for themselves and draw their own conclusions from the audit.”[Clause 1.3 and 1.6 of the Report]. The independent accountants effectively washed their hands off their report and exempted themselves from its effects towards third parties. They were mandated to collate data on foreign currency receipts, payments and deposits transacted between July 2008 and August 2009 and to analyse, review and reconcile such payments and receipts to the cash banked and on-hand at the end of the period and then quantify any prejudice suffered by the appellant.

Their methodology involved interviewing key staff and seeking corroboration of their versions. They studied the cash payments cycle and the receipting and banking system of the appellant. The independent accountants captured the receipts and payments made during the period and reviewed supporting documents and prepared foreign currency cash reconciliations in order to establish if there were any variances. The key staff interviewed were the systems administrator and the bookkeeper.

<u>The systems administrator</u>

She performed the duties of a bookkeeper before one was engaged and was in that capacity the custodian of foreign currency cash between July and 10 November 2008. She locked the cash in a bag which was in turn locked in a safe. The keys to the lockable bag were in the custody of the systems administrator and the managing director. These were the only two people who could unlock the bag. The safe was located under the front reception counter. The keys to the safe were in the custody of a credit controller and the managing director and these were the only two people who could unlock the safe. She required the assistance of either the managing director or the credit controller to access the safe.

She maintained a manual cash book, updated to October 2008, where she was supposed to record all cash payments as they occurred. Apart from the manual cash book she would at times write payments on some pieces of paper while at other times she did not make any record of some of the cash payments. She handed over these duties to a bookkeeper on 10 November 2008. Between the last update in October 2008 and the undocumented handover to the bookkeeper on 10 November 2008, no transactions were recorded in the manual cash book. At no stage were formal receipts ever obtained for third party payments.

The systems administrator could not recall date of handover to the bookkeeper. She did not know the amount she handed over for the simple reason that the two did not conduct a cash count on handover nor record and sign the cash handed over.

The Bookkeeper

She had a safe in her office. The keys to this safe were kept by the managing director and herself. In her time, the two of them were the only persons who had the keys to the lockable bag in which the money was kept before it was locked in the safe. The systems administrator handed over the cash to her in batches without counting it. She did not record or count the money. She did not maintain any record of the cash deposited in her safe. She conducted a cash count of the money on hand on 16 December 2008 at the request of "the director". Between that date and 31 August 2009 she did not record the results of other cash counts that she allegedly did. She did not maintain any cash control record and so she did not know how much she had in the lockable bag at any given time. She did not use the cash book to record cash payments but raised cash vouchers for paying out cash to third parties. No receipts were obtained from these third parties as they were expected to acknowledge payment by signing on the cash voucher.

Comparison between the rules of the Special Court and Order 29 of the High Court rules

The rules applicable to an appeal made in terms of s 65 of the Income Tax Act are set out in the Twelve Schedule of that Act. Rule 1, 7 and 8 are relevant. They provide that:

> "1. The Special Court shall have all the powers of the High Court as in civil actions, and the general procedure and practice, save as specially provided for by these rules, shall be that prevailing in the High Court, in so far as the same is applicable, and if any matter should arise which is not contemplated by either such procedure and practice or these rules, the Special Court shall give instructions regarding the course to be pursued, which instructions shall be binding on the parties.

7. The appellant and the Commissioner may agree to a statement of facts, each setting out his respective contention in law based on such facts, in the form of an agreed case.

8. The agreed case shall be transmitted to the Special Court by the Commissioner within fourteen days of submitting the agreed case to the appellant in terms of rule 6, and the arguments on appeal and the decision of the Special Court shall be confined to the facts admitted."

The Special Court is imbued with the powers exercised by the High Court in civil trials. In addition it is obliged to apply the general procedure and practice prevailing in the High Court where the rules in the Twelve Schedule make no provision for the contemplated procedure and practice. My understanding of the additional provision is that the rules set out in the Twelve Schedule on general practice and procedure override those set out in the rules of the High Court. Rule 7 allows the appellant and the Commissioner to come before the Special Court by way of an agreed case. Rule 8 confines the arguments of the parties and the determination of the Special Court to the agreed facts, which in my view comprise of the any annexures attached to such facts and the rule 11 documents or their equivalent.

In my view, the agreed case in the Special Court is equivalent to a special case provided in Order 29 of the High Court Rules. Rule 199 and 204 read:

"199. Special case by consent
(1) The parties to a civil action or suit may, after summons has been issued, concur in a statement of the questions of law arising therein in the form of a special case for the opinion of the court.
(2) Every such special case shall be divided into paragraphs numbered consecutively, and shall concisely state such facts and documents as may be necessary to enable the court to decide the questions raised thereby.
(3) Upon the argument of such case, the court and the parties shall be at liberty to refer to the whole contents of such documents, and the court shall be at liberty to draw from the facts and documents stated in any such special case any inference, whether of fact or law, which might have been drawn therefrom if proved at a trial.

204. Judgment without hearing evidence
If the question in dispute is one of law, and the parties are agreed upon the facts, the facts may be admitted and recorded at the trial and the court may give judgment without hearing any evidence"

It seems to me that while I am confined to the statement of agreed facts submitted by the parties in this case, I am in terms of the provisions of r 199(3) of the High Court rules at liberty to use the contents of the annexures referred to not only in the statement of agreed facts but also to the r 11 documents or their equivalent comprising the additional annexures filed in the Commissioner's case and draw from them inferences of both fact and law.

In para 8(a) of the statement of agreed facts the parties agreed that a theft occurred in the sum of US$93 459-00 which theft constituted the loss sustained by the appellant. It does not appear to me that this agreed fact is borne out by the results of the appellant's investigation as set out in annexures A and B of the Commissioner's case. The independent accountants literally disowned their report, annexure B. I am unable to find from that report that the appellant suffered a loss in the sum of US$93 459 or even for that matter in any sum.

The report of the independent accountants

The independent accountants accessed receipt books, cash payments supporting documents, bank deposit slips and bank statements from which cash reconciliations for three distinct periods were prepared. The periods were from July 2008 to 10 November 2008. The latter date marked the handover date by the Systems Administrator to the Bookkeeper. The second was from 11 November 2008 to 16 December 2008, the latter being the date the Bookkeeper first counted the money on hand and the third period was from 17 December 2008 to 31 August 2009, the Bookkeeper period to year end.

The appellant transacted in four currencies. The cash receipts were receipted by a cashier. At the end of each day the cashier handed over the cash to the Credit Controller who reconciled the cash to the receipt books and produced a daily cash summary report. The daily cash summary report together with the cash were surrendered to the Systems Administrator in the period July 2008 to 10 November 2008 and to the bookkeeper after 10 November 2008 to 31 August 2009. The Systems Administrator and the bookkeeper acknowledged receipt of the cash and the accuracy of the daily cash summary report by signing on the report. The Systems Administrator and after her the bookkeeper kept the cash in a safe under the reception counter and in her office, respectively. The cash was not deposited into a formal bank account.

The detailed cash reconciliation and summary of the alleged shortfalls for each of the three periods are reproduced below. The opening cash balances in the four currencies accepted by the appellant were on 1 July 2008 derived from the manual cash book maintained by the Systems Administrator. The closing balance on 10 November 2008 was allegedly derived from the cash count conducted by the new bookkeeper of all the cash on hand on that day. This averment by the independent accountants is contrary to the interview reports of both the Systems Administrator and the Bookkeeper to the effect that the money in the lockable bag in the safe was not counted. What the new bookkeeper could possibly have counted was the cash surrendered to her by the credit controller on that day as recorded in the daily cash summary report. Again, the closing balance of 16 December 2008 was derived from the cash count on that date that was carried out by the Bookkeeper. The closing balance of US$3 738 was derived from the cash count that was carried out on 31 August 2009.

"3. Detailed findings

3.1 Cash reconciliation 1 July 2008 to 10 November 2008

	US$	ZAR	GBP	EUR
Opening cash balance as at 1 July	5 088	4 400	162	320
Receipts	220 403	31 465	1 725	130
Quotation deposits receipts	500	-	-	-
Payments	(31 572)	(14 050)	-	-
Cash banked	(56 900)	-	-	-
Cash balance	(55 200)	(11 000)	(160)	
Cash shortfall on 10 November 2008	**82 319**	**10815**	**1727**	**450**

3.2 Cash reconciliation 11November 2008 to 16 Dec 2008

	US$	ZAR	GBP	EUR
Opening cash balance[1]	55 200	11 000	160	-
Receipts	118 000	45 850	779	110
Quotation deposits	300	-	-	-
Payments	(193 719)	(28 995)	-	-
Cash banked		-	-	-
Cash balance per count on 16 December 2008	(31 323)	(24 110)	-	-
Cash (surplus)/shortfall 11/11/2008 to 16/12/2008	**(51 542)**	**3 745**	**939**	**110**
Cash shortfall (1 Jul to Nov 2008)	**82 319**	**10 815**	**1 727**	**450**
Cumulative shortfall on 16/12/2008	**30 777**	**14 560**	**2 666**	**560**

Over the second period payments in cash were in excess of cash available. The explanation in para 3.1 of Annexure A to the Commissioner's case was that the Systems Administrator handed cash to the Bookkeeper in batches without counting, recording and signing for it. The excess payments comprised cash that was received by the bookkeeper

[1]Prior period cash count balances were paid as opening balances for this period thereby factoring out previous unaccounted for balances.

from the Systems Administrator. The bookkeeper found herself with money that she could not reconcile to source documents.

3.3 Cash reconciliation 17 December 2008 to 31 August 2009

	US$	**ZAR**	**GBP**	**EUR**
Opening cash balance on 17/12/2008	31 323	24 110	-	-
Receipts	757 037	143 990	3 035	1 180
Quotation deposits	-	-	-	-
Payments	(317 432)	(21 520)	-	-
Cash banked	(411 920)	(106 140)	(1 440)	-
Cash balance that should be available	**58 008**	**40 440**	**1 595**	**1 180**
Cash count balance on 31/08/2009	**3 738**	**4 620**	**20**	**0**
Cash shortfall 17/12/2008 to 31 08/2009	**54 270**	**35 820**	**1575**	**1 180**
Cash shortfall 16/12/2008	**30 777**	**14 560**	**2 666**	**560**
Total cash shortfall 1 July 2008 to 31 August 2009	**85 047**	**50 380**	**4 241**	**1 740**

<u>Summary of the alleged shortfalls</u>

	Amount of shortfall			
Period	**US$**	**ZAR**	**GBP**	**EUR**
01/07/2008 – 10/11/2008 (to hand over date)	82 319	10 815	1 727	450
11/11/2008 – 16/12/2008 (to Bookkeeper's first count date)	(51 542)	3 745	939	110
17/12/2008 – 31/08/2009 (Bookkeeper period to year end)	54 230	35 820	2 280	430
Total prejudice to organisation	**85 007**	**50 380**	**4 946**	**990**

The report revealed two major weaknesses in the cash management system of the appellant. The first was the absence of regular surprise cash counts over the whole period in question. The second was that a proper cash book was not maintained. The amount of cash on hand at any given time could not be ascertained. After the engagement of the bookkeeper, cash counts were allegedly done on 31 October 2008 for United States dollars only and on 10 November 2008 for all the four currencies and lastly on 11 November 2008 for United Sates dollars and South African Rands. Thereafter the only other documented counts were carried out on 31 August 2009. The independent accountants noted in clause 4.1 of their report that "management indicated that further counts were done but these were not recorded or reconciled to separate cash book records". In some instances there were no third party supplier supporting documents for cash payments made to third parties and in the instances involving the sums of US$5 792-00 and ZAR 9 000-00 they were content to rely on the verbal assurances of "the director" that they constituted genuine expenditure. In some cases expenditure was represented by amounts written on pieces of paper on file without any payment vouchers or requests or authorisations from senior authorised officials.

Whether a loss or a theft was established

It does not seem to me that the statement of agreed facts as read with the annexure A and B established that a theft occurred. In the absence of a properly maintained cash book, it is difficult to find that cash payments that constitute the unaccounted funds were not made in the course of business. They may very well have been made and not recorded by both the systems administrator and bookkeeper whose duty it was to do so. The evidence established that the systems administrator did not record in the cash book or on pieces of paper some of the payments that were made to third parties. It also established that when the bookkeeper was engaged she did not keep a cash book at all. Rather she raised cash vouchers for paying out cash to third parties, which the third parties were expected to sign in acknowledgment of payment. The impression made being that some of the third parties did not sign these vouchers.

On the evidence deposed in the independent accountants report, I am not satisfied that the appellant has demonstrated on a balance of probabilities that the cash discrepancies noted therein constituted a loss by theft of the appellant's foreign currency receipts. The agreed fact that at all material times, therefore, there was a real risk of the misappropriation of funds occurring given the state of the economy and the dire need for services, and the theft suffered was incidental to the carrying on of the appellant's business activities and inseparable therefrom would have been relevant had the loss or the theft been proved on a balance of probabilities.

Section 15 (2) (a) of the Income Tax Act provides that:

> "(2) The deductions allowed shall be—
> (*a*) expenditure and losses to the extent to which they are incurred for the purposes of trade or in the production of the income except to the extent to which they are expenditure or losses of a capital nature;"

In the absence of oral evidence, the Court is not privy to the purposes for which these funds were used. We do not know whether the payments were in respect of purchases of capital equipment or stock-in-trade. The claim for deduction based on the alleged existence of a cash discrepancy must therefore fail. I would dismiss the appeal on this basis.

The second difficulty that confronted me in determining this matter lay in the concession made in oral argument that the managing director was not one of the possible defalcators of the cash. The removal of the managing director from possible suspicion was made for the first time by Mr *Girach* in oral argument. It was not based on any averment in the statement of agreed facts. It was not hinted in the sole issue referred for determination of the stated case. The agreed facts indicated that the *modus operandi* of the theft and the identity of the thief could not be established by the appellant or the investigation by the independent firm of accountants. The parties merely excluded the involvement of a shareholder or anyone with a direct interest in the business of the appellant from the theft.

<u>The validity of the exclusion of the managing director</u>

In the objection of 13 February 2012, the tax consultants of the appellant underscored the point that the discrepancy comprised funds of the company misappropriated by a member or members of staff of the company whose identity could not be ascertained. At p 2 of the objection they contended that:

> "In your interactions with the company you have alleged the deduction to be non-allowable on the grounds that the person or persons who misappropriated the funds will have been management personnel, but it is respectfully submitted that that does not render the deduction non-allowable, and particularly so as such person or persons were employees, but not a shareholder or shareholders in the company."

And in the ruling of 18 May 2012 disallowing the objection on the cash discrepancy the respondent wrote:

> "It is not disputed that your client discovered cash discrepancies as evidenced in the report by the firm of auditors. I have however gone through the report and noted that the Bookkeeper, Systems Administrator, Credit Controller and the Managing Director all had access to the keys to the lockable bag and or the places where the cash was kept. In this case it is not known whether it was the employees or managers who could have caused the cash discrepancies. However management has the responsibility of ensuring that controls are in place in order to ensure that such embezzlements do not take place. A distinction should be drawn between a loss suffered due to embezzlement of cash by employees and managers or proprietors. In the case of a manager or proprietor, such losses are not allowable. In this case I did not find any conclusive information that the cash discrepancies were caused by employees."

In para 42 to 50 of the Commissioner's case the above contention is reinforced. In fact in para 46 and 47 the Commissioner contended that the likelihood of the managing director having taken the cash was high. The basis for excluding the managing director was not revealed to me in argument. The concession in regards to the managing director that was made Mr *Magwaliba* runs contrary to the attitude adopted by the Commissioner before the statement of agreed facts was reached and to the statement of agreed facts and issue referred for determination. It is certainly not supported by the annexures equivalent to r 11 documents filed of record. The parties did not take the court into their confidence on the basis for the exclusion. In the absence of such a basis I am unable to hold that the concession was properly made.

The sole issue referred for determination in the stated case

The sole issue for determination is whether or not an employer who suffers a loss in consequence of a theft of monies which is perpetrated by a person or persons other than a shareholder, or an owner and such theft occasions loss to his business, is entitled to a deduction under s 15 (2) (a) of the Income Tax Act [*Chapter 23:06*].

The onus

In terms of s 63 of the Income Tax Act and case law the onus lies on the taxpayer to prove on a balance of probabilities that the Commissioner was wrong in disallowing the deduction of the sum of US$93 459. In *ITC* 1221 (1974) SATC 233 at 235 Whitaker P on the authority of Beadle CJ in *Commissioner of Taxes* v *Rendle* 1965 (1) SA 59 (SRAD) at 65F-H 26 SATC 326 said:

> "It is now well settled that before fortuitous expenditure resulting from a mishap which has befallen a taxpayer can be deducted as expenditure incurred for the purpose of trade the taxpayer must show that the risk of mishap which gave rise to the expenditure was inseparable from or a necessary incident of the carrying on of his business."

To the same effect is Watermeyer J in *ITC 1242* (1975) 34 SATC 306 (C) at 309 that:

> "Before a taxpayer can succeed he must show that the risk of the loss which he seeks to deduct from his income is inseparable from, or a necessary ingredient of the carrying on of the particular business. If it is, then to use the language of Watermeyer AJP *in Port Elizabeth Tramway* case, *supra*, as modified in the subsequent cases referred by Beadle CJ, it would be proper, natural or reasonable to regard the loss as part of the cost of performing the business operations *bona fide* performed for the purpose of earning income."

See also Roper J in *ITC* 815, 20 SATC 487 at 493:

> "It is immaterial therefore that in paying out moneys in order to settle a liability or loss the taxpayer has not done an act directed to the production of income. The question is whether he incurred the loss or liability which caused him the loss, in the course of operations directed to the production of income. Where the liability or the loss has arisen as a result of mischance or accident the further question arises whether the nature of the taxpayer's business is such that the risk of such a mishap can be said to be inseparable from or necessary incident of, the carrying on of the business."

The non-exclusion of the managing director from the list of possible defalcators would be fatal to the appellant's case. In our jurisdiction misappropriations by a managing director are excluded from deduction as losses on the ground that they are not regarded as a necessary incident or inseparable from the taxpayer's trading activities. The rationale against such deductions provided by Fieldsend P in *ITC* 952 (1962) 24 SATC 547 at 551 was that it was not reasonably expected for a managing director by virtue of his position to make away with his employer's funds. Beadle CJ in *Commissioner of Taxes* v *Rendle* at 65F-H cited with approval Gunn's *Commonwealth Income Tax Law and Practice* 7 ed p 617 that:

> "Where a loss arises in the course of carrying out a necessary or expedient part of the operations directed to the gaining of the assessable income of a business, the loss is an allowable deduction under sec. 51 (*Ronpibon Tin No Liability v Federal Commissioner of Taxation,* (1949) 78 C.L.R. 47; 4 A.I.T.R. 236; C*harles Moore & Co. (W.A.) Pty. Ltd v Federal Commissioner of Taxation,* (1956) 6 A.I.T.R. 379). The handling of loan moneys and other trust funds is an essential part of a solicitor's practice; this work is necessarily entrusted to clerks, and losses arising from embezzlement of trust funds by a clerk constitute 'a familiar and recognised hazard' (6 A.I.T.R. at p. 385) incidental and relevant to the gaining or producing of the solicitor's assessable income. If the loss is occasioned through the acts of a clerk or other employee of the taxpayer (be it 'purloinings by office boys' or embezzlement by a managing clerk) the loss may be deductible under sec. 51, <u>but if the wrongful act is committed by a proprietor, including a partner, no deduction is permitted under that section. Between these two classes of persons a line has been drawn by the courts, namely where the loss is occasioned through the acts of a managing director or a manager of a company who 'is in the position of a proprietor' the proprietor has been denied a deduction of the loss</u>.'
>
> <u>I consider this statement of the law to be applicable to cases under our Income Tax Act."</u>(Underlining my own for emphasis).

The case is regarded by textbook writers as the leading case in the field of deductions of embezzled funds both in Zimbabwe and South Africa. Hill in *Income Tax in Zimbabwe* 3ed 1993 at p 60 recognizes the primacy of *Rendle's* case and states that:

> "It is clear on authority that losses resulting from thefts by a managing director, a director or a manager in the position of a proprietor are not losses which can be regarded as losses which are an incident of the taxpayer's trading activities."

And *Silke: South African Income Tax* 17thed 2015 para 7.10.14 at p 162 [and 16th ed 2014 at p161-2] writes:

> "In *COT* v *Rendle* (1965 AD) the Appellate Division of the High Court of Rhodesia referred to the inconsistency of decisions relating to this matter. The Court had sanctioned the deductions of misappropriations of money belonging to clients of the taxpayer by his employees. Its reasoning leaves one in no doubt that embezzlements and thefts of cash whether by employees, burglars or armed robbers constitute an allowable loss for tax purposes except when an employee is a managing director or a manager since the risk of theft by such an employee can hardly be regarded as being a necessary concomitant of the business activities. The principle is the following:
>
> a. if the loss is due to defalcations by the managing director or owner of the business, it is not allowed as a deduction (*Lockie Bros Ltd v CIR* (1922 TPD)

> b. losses suffered due to defalcations by subordinate employees will be allowed as a deduction since the risk of theft by such employees can be regarded as being a necessary concomitant of the business activities. These losses generally arise from a risk that is always present when subordinate employees are engaged in performing the duties entrusted to them."

The case has also been cited with approval by Whitaker P in the local case of *ITC 1221* (1974) SATC 233 at 235, and by Watermeyer J and Hill AJ in the two South African cases of *ITC 1242* (1975) SATC 306 (C) at 309 and 310 and *ITC* 1383 (1978) 46 SATC 90 at 94, respectively.

The appellant has failed to validly exclude the managing director from the possible list of defalcators. I would also dismiss the appeal on this basis.

The last leg upon which I am obliged to determine the matter is the one argued by the parties based as it was on the statement of agreed facts and the concession made in oral argument. It will be recalled that that the parties agreed that a loss arising from theft visited the fortunes of the appellant and further that the managing director was not one of the possible embezzlers.

Mr *Girach* submitted that the appellant was entitled to the deduction as the theft was occasioned by some unknown employee of the appellant who was not the managing director, or director or shareholder or a manager in the position of a proprietor. Mr *Magwaliba* on the other hand submitted that our law did not permit a deduction for a theft occasioned by a manager. He contended that the appellant failed to discharge the onus on him to establish on a balance of probabilities firstly that the thief or thieves were not managers of the company and secondly that they were not managers who could be equated to the managing director.

<u>Whether or not the loss arising from theft by a manager is deductible</u>

In Zimbabwe, the distinction in the tax deductibility of a loss due to theft by a manager and a non-managerial employee appears to have been suggested for the first time by Fieldsend J in *ITC 952,* (*supra*). (In that case he was dealing with the deductibility of a loss occasioned by a partner in a law firm. He confirmed the disallowance. He suggested at p 552 that a distinction could be made between the embezzlement committed between ordinary servants on the one hand and managers and managing directors on the other when he stated at p 552 that:

> "If a distinction is to be drawn between ordinary servants and managers and managing directors, for which there appears to be authority, it seems to me that, *a fortiori,* a partner is in quite a different position to an ordinary servant. For that reason alone it seems to me that the appeal in this case cannot be allowed."

The second case that set the clear position in this country was *Rendle*'s case where Beadle CJ adopted the formulation in Gunn, *supra,* as part of our law. He stated that loss occasioned by acts of a clerk or other employee of the taxpayer in the nature and form of purloinings by office boys or embezzlement by a managing clerk may be deductible but not loss occasioned by the wrongful acts of a proprietor or a partner. These two positions constituted the black and white parameters set by the law. Between them was a grey area in which the courts disallowed the deduction of a loss occasioned through the acts of a managing director or a manager of a company who 'is in the position of a proprietor'.

Silke, *supra,* in the third sentence of the quotation cited above suggests that *Rendle*'s case decided that embezzlements or thefts of cash by a managing director or a manager were not allowable tax deductions since the risk by such an employee could hardly be regarded as a necessary concomitant of the taxpayer's business activities. In suggesting that Beadle CJ precluded deductions of a loss occasioned by an employee who is a manager Silke clearly misunderstood the full import of the learned Chief Justice's statement. Apparently Silke was not alone in this mistaken belief. In *ITC 1242* (1975) 37 SATC 306(C) at 309 Watermeyer J also believed Beadle CJ distinguished *Lockie* on the ground that the theft was committed by a manager and not a subordinate employee, a distinction with which he agreed. He too misunderstood Beadle CJ who actually said at 66A-B:

> "*Lockie Bros.,* case, *supra,* can, I think, be distinguished on the grounds in which FIELDSEND, P., distinguished it in case *952, supra* at p. 551. In *Lockie Bros.* case the defalcations were by a <u>managing director</u> and not by a subordinate employee. The risk of theft by a <u>managing director</u> can hardly be regarded as inseparable from the carrying on of the business."(Underlining mine for emphasis)

In his reasoning Beadle CJ treated Cheesman as a managing director even though in reality he was a mere manager. He thus made the distinction as between a managing director and a subordinate employee and not as between a manager and a subordinate employee as suggested by Watermeyer J and imputed by Silke. This is despite the suggestion by Fieldsend P that a distinction could be made between the loss occasioned by a manager and a subordinate employee. It will be recalled that the issue confronting Beadle CJ was the contention at 65C by Mr *Pudney* for the Commissioner purportedly based on *Lockie Bros. Ltd v Commissioner for Inland Revenue,* 1922 T.P.D. 42, and Tax Case 184, 5 SA Tax Cases 268 that "it was not permissible to deduct fortuitous expenditure occasioned by the embezzlement of one of the taxpayer's own employees." The learned Chief Justice dismissed Mr *Pudney's* contention. The only other reference he made to the *Lockie Bros.* case was in disagreeing with Roper J and even with the suggestion by Fieldsend J that the thefts in both *Lockie* and *ITC 815[*deductibility of thefts by an attorney's clerk not proved to have been of trust funds] were of a capital nature.

It is apparent to me that Beadle CJ's dismissal of Mr *Pudney's* argument based on his understanding of *Lockie Bros.* case was consistent with his finding that the Gunn statement of the law was applicable to cases under our Income Tax Act. In my view, the answer to the sub-issue I raised was provided by Beadle CJ at p 65D-E in these words:

> "I can, however, see no logical argument which prevents the broad test which I have just enunciated being applied to the theft by an employee as well as to the theft by a third party. The risk of loss by theft of an employee may be just as great and in some cases greater than the risk of loss by theft of a third party. It cannot be argued that in this instance the employee stands on a different footing from the third party because he is engaged on his employer's business at the time. When he steals from his employer, he is not acting in the execution of his duties - he is,to use the hackneyed legal phrase, 'on a frolic of his own', and vis-à-vis his employer, he seems then to stand on precisely the same footing as a third party, as, for example, the robbers in the *Charles Moore Ltd.* case, *supra*, and in the *Gold Band Services* case, (*supra*)."

The learned Chief Justice, in my view, suggested that embezzlement by ordinary managers who are not excluded in the Gunn formulation would be deductible.

<u>The Lockie Bros. case</u>

The case was decided in 1922. The appeal was presided over by Mason J and de Waal J who came to the same conclusion but for different reasons. The two judges described the employee of the rice trading taxpayer, one Cheesman, as a "manager of the company who had full power to operate its bank account in Johannesburg." He had full power to withdraw money for all purposes incidental to the company's enterprises and not for his own purposes. The incidental purposes were described as the payment of salaries for the manager and clerks, freight charges on rice purchases, rent for offices and shops, costs of stationery, telegrams and stamps. He appropriated to his use large sums of money belonging to the company. He withdrew the money from the company bank account to cover fictitious purchases of rice, misuse of petty cash and transport charges. Mason J disallowed the deductions on the ground that the loss due to the embezzlement was not an operation undertaken for the purposes of business that constituted a loss or outgoing actually incurred in the Union in the production of income. It was not loss due to company operations. De Waal J disallowed the deduction on the ground that the loss was of a capital nature.

De Waal poignantly recognised that the nature and scope of Cheesman employment as a manager required of him to manage the company's business not to steal. He indicated that the computation of income tax was based on setting-off valid purchases against sales with the credit balance constituting income from which income tax would be derived. He considered the money withdrawn from bank to be a capital asset which remained of a capital nature even when converted into stock-in-trade of rice. At p 48-9 he stated that:

> "Once the company's assets are converted into money it becomes portion of its capital for reinvestment, if so desired, in other purchases of rice, and any withdrawal of such capital, whether authorised or not, not for the purposes and objects of the company, would not be a loss or outgoing, and in the case of an illegal or criminal abstraction from such funds, the loss to the owner of such moneys becomes a loss of a capital nature. So soon as any asset of the company is converted into cash, such cash is added to and forms part of the company's capital, and if thereafter such cash or any portion thereof is lost, whether through the negligence or criminal act of the company's servants, such loss becomes a loss of the company's capital: D' Arcy-Irvine pp 130/133. The loss occasioned through Cheesman's defalcations is therefore not a loss incurred in the production of the income of the company, but a loss of a capital nature and cannot be deducted from the income of the company in terms of the Act."

Cases decided subsequent to Lockie Bros.

ITC 1242 (1975) 37 SATC 306 (C) was a case in which two clerks who worked under a chief accountant in a book publishing and selling company made 22 illegal abstractions over a period of 18 months from the company bank account and misappropriated petty cash and payments surrendered to them by other members of staff for banking. A manager testified that the duties of the clerks entailed writing up and balancing the cash book, keeping and balancing petty cash and controlling both the cheque book (which required two signatories). The two clerks drew cheques on the company bank account and destroyed them on return from the bank and ordered personal goods in the firm's name. Watermeyer J held that the risk of this kind of loss was ever present from subordinates entrusted with the duties carried out by the clerks. He found the risk of the loss happening was inseparable from the appellant's business activity and concluded that the loss was incurred in production of income. In essence, unlike De Waal J, Watermeyer J did not treat as a capital asset money in a taxpayer's bank account.

In *ITC 1383* (1978) 46 SATC 90 (T) the taxpayer was a commercial bank. A general manager of the bank gave uncontroverted evidence. The bank secretary who doubled as the staff manager and was the 6th highest ranking official in the bank stole part of the floating capital of the bank. He was in charge of 3 people consisting of his personal secretary, a receptionist and a clerk. His authority entailed signing vouchers for staff salaries. He signed vouchers creating false credit entries and appropriated withdrawals to his own use. The Commissioner contended firstly that only petty pilfering by junior employees was deductible in computing taxable income and not theft by any other employee and secondly that fortuitous loss was not deductible unless the taxpayer established that the risk giving rise to the loss was inseparable from or a necessary incident of conducting his particular business.

Hill AJ found firstly that commercial banks required employees whom it entrusted with its funds to pursue its business objectives and secondly that the risk of embezzlement by such employees was incidental to all business just like pilfering of stock and theft of cash from the till, negligent handling of goods and negligent conduct of businesses, which were well known and common sources of loss. He held that the risk of theft by bank employees who must necessarily handle large sums of money however stringent selection and supervision was an ever-present factor in the administration of its business and must be regarded as inseparable from it.

ITC 1221 (1974) 36 SATC 233 (R) was a local appeal in which Whitaker P described the secretary and accountant of a departmental store as a senior employee whom he, however, categorised as a subordinate employee based on his job description. This senior but subordinate employee held no proprietary interest in and was not a director of the taxpayer. His duties entailed keeping books of account, signing cheques, supervising office administration, ordering office stationery and equipment, paying staff salaries, hiring and firing junior staff, attending to customer complaints and in the absence of the managing director on leave attending to requests for donations and advertising. Whitaker P was prompted by the authority of *C of T* v *Rendle* (*supra*); *Bamford (Inspector of Taxes) ATA Advertising Ltd* [1972] 3 AllER 535 at 544, *Curtis* v *J&G Oldfields Ltd* 41 TRL 373 at 374, *IT Case 952,* 24 SATC 547; *Gunn Income Tax Law and Practice* 8 ed vol 2 para 51/95 p 204to hold that the loss from thefts committed by a managing director or director or manager in the position of proprietor were not losses connected with or arising out of trade while thefts committed by subordinate employees could be regarded as losses which were an incident of the taxpayer's trading activities.

He found the risk of embezzlement by the secretary cum accountant was an ever present incident of the business activities of appellant that constituted a familiar and recognisable hazard and the ensuing loss was sufficiently closely linked to it so as to form the cost of doing business. He based this decision on two factors. Firstly, that it was necessary to employ a secretary cum accountant and secondly that keeping a bank account was a necessary incident of the appellant's trading activity and loss occasioned by the abstraction of funds from this account was intrinsic to its trading activities. He took judicial notice of these factors to dispose of the Commissioner's argument that the appellant had failed to discharge the onus on him to show that the loss was inseparable from its trading activities.

The common thread that runs through each of these three cases was that the taxpayer suffered loss as a result of thefts perpetrated on its banked funds by an employee who was not a managing director, a director, a proprietor or a manager in the position of a proprietor. All the judges who decided each of these cases, unlike De Waal J held that the banked funds constituted floating or circulating capital and not fixed capital and allowed the deduction of the loss arising from the theft in the computation of each taxpayer's taxable income. These views found repose in *CIR* v *George Forest Timber Co Ltd* 1924 AD 524 and *New State Areas Ltd* v *CIR* 1946 AD 620. In the latter it was said in contradistinction to De Waal J's sentiments that:

> "When the capital employed in a business is frequently changing its form from money to goods and vice versa like in the purchase of and sale of stock by a merchant or purchase of raw materials by a manufacturer for conversion to a manufactured article, and this is done for profit, the capital employed is floating capital. The expenditure of a capital nature prohibited by [the South African equivalent of our s 15 (2) (a)] is expenditure of a fixed nature not expenditure of a floating capital nature, because expenditure of floating capital to earn a profit such as purchase of stock-in-trade, must necessarily be deducted from the proceeds of the sale of the stock-in-trade in order to arrive at the taxable income derived by the taxpayer from that trade."

The bank secretary in *ITC 1383* was also a staff manager. The secretary and accountant of the departmental store in *ITC 1221* was a in my view a senior managerial employee who carried out some of the functions of the managing director when he was on leave. The defalcations of these two senior managerial employees were allowed as deductions in the computation of the income tax of their respective employers.

It seems to me that the final nail against the contention by Mr *Magwaliba* that the loss occasioned by the defalcations of managerial employees is not deductible was put to rest by Beadle CJ in Rendle's case at p65D where he could not comprehend any argument which prevented the application of the broad test in respect of deductions for fortuitous losses arising from the theft by an employee just as it was applied to a third party as was the case in *Charles Moore and Gold Band* cases. In *Charles Moore & Co (WA) (Pty) Ltd* v *Commissioner of Taxation* (1956) 6 AITR 379 the money lost to robbery comprised of cash received from the sale of stock-in-trade, payments of customer's accounts rendered monthly, payments from goods ordered and despatched by mail by customers for letters of credit, payments of deposits and periodic payments of lay-by accounts, payments received on staff ledger accounts of goods purchased by employees and cash payments received in the ordinary course of business. The law he propounded for Zimbabwe was that a deduction is denied of the loss occasioned by the wrongful acts of a proprietor, including a partner, and through the acts of a managing director or a manager of a company who 'is in the position of a proprietor'. Cases with persuasive authority such as *ITC 1242* and *ITC 1383* have added a director to that list. It is therefore clear to me that embezzlement by ordinary managers who are not excluded in the Gunn formulation would be deductible.

<u>Whether the systems administrator and bookkeeper were managers</u>

Mr *Magwaliba,* further submitted that the appellant had failed to discharge the onus on it to show on a balance of probabilities that the systems administrator and bookkeeper were not managerial employees. In his oral submissions Mr *Girach* actually described the two employees as mere accountants and contended that para 8 c of the statement of agreed facts did not identify them as managers. In my view the onus was on the appellant to establish that the two employees were not managers. Para 8 c of the statement of agreed facts does not describe the two as managers nor does it describe them as non-managerial employees. In its ambivalence para 8 c is capable of holding both meanings. I agree with Mr *Magwaliba* that as the appellant has failed to discharge the onus it bears, the meaning that is contrary to its submission must carry the day. I find that they were managerial employees.

<u>Whether the systems administrator and the bookkeeper were managers in the position of a proprietor or managing director</u>

In both his written and oral submissions, Mr *Magwaliba* did not address the question whether the systems administrator and bookkeeper were managers in the position of a proprietor. Rather, he argued that they were managers in the position of a managing director whose defalcations were not deductible. The phrase 'manager in the position of a proprietor' was not defined by Beadle CJ in *Rendle's* case. It must have been uplifted from some decided case or cases by Gunn. I failed to access Gunn and was therefore unable to ascertain the genesis of the phrase. It seems to me that the phrase has much in common with the concept of ostensible authority in the law of agency and that of quasi-mutual assent in the law of contract. In my view, a manager in the position of a proprietor is not as a matter of hard fact a proprietor. Neither is a manager in the position of a managing director in reality a managing director. Such a manager is imputed to be a proprietor or a managing director by virtue of his words or conduct.

I have already stated the import of my understanding of Beadle CJ's remarks at p 66A-B. While Cheesman was a manager, in the words of Hill AJ in *ITC 1383* at p 92, "with full plenary powers to represent his in employer", of an English company operating in South Africa, Beadle CJ equated his authority with that of a managing director. It would appear to me that Mr *Magwaliba's* contention that the systems administrator and bookkeeper were managers 'in the position of a managing director' is rooted on firm ground. Mr *Girach* submitted that the two employees could not be equated to a managing director who in his contention was "in charge of the whole business". There was as aptly described by Mr *Magwaliba*, a "paucity of evidence" in the statement of agreed facts. The statement of agreed facts does not describe the nature and scope of the system administrator and the bookkeeper's duties and authority. If indeed I am confined to the four corners of the statement of agreed facts in resolving the issue before me, then the appellant faces the insurmountable task of establishing that the two did not possess the plenary powers of the managing director. The statement is also silent on the nature and scope of the managing director's duties and authority. There are no facts in the statement of agreed facts to establish on a balance of probabilities that the two did not possess the powers and authority of the managing director. The result would be the same in the determination of whether or not the two were managers 'in the position of a proprietor'. I would thus find against the appellant on this point.

In his reply to the oral submissions of Mr *Magwaliba*, Mr *Girach* contended that the money could have been stolen by other employees besides the systems administrator or the bookkeeper such as the cashiers as during the course of the day various people had access to the safe. He was clearly giving evidence from the bar as the alleged course of conduct was not disclosed in the statement of agreed facts. The evidence from the bar was however contrary to para 4.1 of the report of the independent accountants, annexure B. The cashiers surrendered the cash and receipt books to the credit controller. The credit controller reconciled the cash to the receipt books and produced a daily cash summary report. He in turn surrendered the cash and the daily summary report to the systems administrator and after her engagement the bookkeeper. The recipient of the cash would acknowledge the receipt and accuracy of the cash by appending her signature on the daily cash summary report. It was again contrary to annexure A which stated that the custodian of the keys to the lockable bag were the cash was kept before the engagement of the bookkeeper were the systems administrator and the managing director while the safe key in which the money was banked was kept by the credit controller and the managing director. After the engagement of the bookkeeper both keys to the lockable bag and safe were in the custody of the bookkeeper and the managing director. In my view, the only people who could access the money in the bag were the systems administrator, the bookkeeper and the managing director. The credit controller could not do so as he did not have custody of the key to the lockable bag.

The import of the evidence in annexure A and B is that during her time, the system administrator could not access the safe without the collaboration of either the credit controller or the managing director. The credit controller, even though he had the keys to the safe, could not access the lockable bag with the money as he was not in custody of the key to this bag. The managing director could access both the bag and safe on his own. If he is excluded from the possible suspects, the only person who would remain under suspicion would be the systems administrator. She conducted herself in a very tardy manner. She was not supervised at all. It does not appear that she placed all the cash in the lockable bag as on handover to the bookkeeper, she did not give her all the cash in her custody at once but in at least three batches. Further, the second period reconciliation where the bookkeeper made more payments than were justified by the cash she received as recorded in her daily cash summaries confirms that the systems administrator who provided her with the excess funds did not keep all the cash she received in the lockable bag. She did not conduct cash counts or record some of the payments she made in the cash book. In the period of the bookkeeper the exclusion of the managing director from suspicion leaves the bookkeeper in the lurch. It does not appear that she was under the supervision of anyone. She only conducted a cash count on 16 December 2008 at the request of the director and thereafter does not appear to have done so. She did not conduct a properly supervised handover takeover with the systems administrator.

The impression left by the conduct of both the systems administrator and bookkeeper but especially the bookkeeper was that they were unaccountable independent centres of power and authority in the appellant company. They behaved and were permitted to behave as managers in the position of a proprietor. A proprietor, as the owner of the business especially of a small private business would appear to have wide latitude to do as he pleases especially with the money in his business. The making of drawings from the business does not invite opprobrium from anyone and no report is made to law enforcement agents to bring the owner to book for 'misappropriating' his funds. The approach to the investigation was lackadaisical. It seems the appellant was not keen to identify the culprits and bring them to book. It behaved as if it was afraid to confront the proprietor of the company. The cumulative impact of these factors is that the managers who stole the money were managers in the position of a proprietor.

Conclusion

In the final analysis, it does not really matter whether I am wrong in disregarding the statement of agreed facts and concession made in argument removing suspicion from the managing director; I would still dismiss the appeal on the ground that the appellant failed to discharge the onus on it to show on a balance of probabilities that the systems administrator and bookkeeper were not managers in the position of a managing director or a proprietor.

Penalty

Mr *Girach* did not make any submissions in respect of the penalty. I assume that he abandoned the appeal in that regard. I would be inclined to impose a similar penalty for the reasons advanced by the respondent. In its favour the appellant fully co-operated with the respondent throughout the entire investigation. In aggravation it initially wrongly sought to deduct the provision for audit while at the same time disallowing provision for bad debt notwithstanding that the two stood on the same legal footing. The cash was most likely used in the operations of the business but if it was not it was most likely stolen by one or all of the possible three suspects who were in custody of the keys to the lockable bag and safe.

Costs

I am satisfied that the grounds of appeal raised by the appellant were frivolous. It does not seem to me that the appellant ever had an arguable case in this matter. This is a clear case crying out for an award of costs to the Commissioner. I will therefore award costs to the Commissioner on the ordinary scale.

Disposition

Accordingly, it is ordered that:

1. The appeal is hereby dismissed.

2. The amended assessment issued by the Commissioner on 7 February 2012 for the tax year ended 31 December 2010 is confirmed.
3. The appellant shall pay the costs of the Commissioner on the ordinary scale as taxed by the registrar.

Atherstone and Cook, appellant's legal practitioners