30/96

CG CASE NUMBER: 348/94

IN THE SUPREME COURT OF SOUTH AFRICA

(APPELLATE DIVISION)

In the matter between:

SAPPI CAPE KRAFT (PTY) LTD Appellant

and

COMMISSIONER FOR INLAND REVENUE Respondent

CORAM: **BOTHA, HEFER, NESTADT, HARMS JJA et PLEWMAN AJA**

HEARD ON: **23 FEBRUARY 1996**

DELIVERED ON: **27 MARCH 1996**

J U D G M E N T

PLEWMAN AJA

The appellant Sappi Cape Kraft (Proprietary) Limited carries on business as a manufacturer of paper at Milnerton, Cape Province. Appellant was at all relevant times registered in terms of Section 12 of the now repealed Sales Tax Act 103 of 1978 ("the Act") as a vendor in respect of a manufacturing enterprise.

In the course of the manufacturing activities undertaken by appellant it purchased locally and it imported into South Africa parts or materials which can be identified for the purpose of this appeal as "screen plates", "under and top wires" and "wet and dry felts". At earlier stages of the proceedings claims relating to other items of expenditure incurred in its manufacturing processes namely the hire of cranes and the purchase of boiler chemicals were also in dispute between the appellant and the respondent, the Commissioner for Inland Revenue. So, too, was a question of certain penalties levied by the respondent. These questions have fallen away. The only question in the appeal is whether the respondent's assessments of the appellant in respect of sales tax payable

in terms of the Act in the years 1983 to 1987 were correctly made.

The assessments were raised after an inspection by a representative of the respondent of the appellant's premises. The detail of how this came about and what transpired thereafter is irrelevant. The assessments having been raised they were objected to and the objections in due time were disallowed. The appellant then appealed to the Income Tax Special Court. That court, after hearing evidence and argument, made an order on 17 August 1992 upholding the objections made in respect of transactions involving under and top wires but confirmed the assessments in respect of transactions involving screen plates and wet and dry felts. The appellant then appealed to the Cape Provincial Division. The respondent cross appealed in respect of those transactions on which it had failed.

The full court of the Cape Provincial Division upheld the appeal by the appellant in respect of the transactions relating to dry felts but dismissed the appeal relating to wet felts. The cross-appeal in respect of

under and top wires was upheld. The appellant now comes on appeal to this Court against that part of the order made which is adverse to it. What then is in issue in this appeal is whether the purchases of wet felts, screen plates and under and top wires by the appellant were exempt from sales tax.

There was argued before this Court on the same day as the present appeal was heard an appeal by Mondi Paper Company Limited ("Mondi") vs Commissioner for Inland Revenue involving similar questions of law and fact. Mondi is also a manufacturer of paper. In that case, as in this case, evidence was led to explain the paper making process. In a judgment in the Mondi case to be delivered at the same time as this judgment, there is set out a description of the paper making process. What is there said is adequate to give a broad understanding of the process also for the purposes of this appeal and I therefore do not again summarise here the evidence given in this case explaining the process which did not in this respect present any distinguishing features. Indeed

Mondi's plant it seems is very similar to the appellant's and the items of equipment in issue are for all practical purposes identical to those in issue in that case.

The Act has since been repealed but it was at the relevant time a much amended statute - this was especially so with the list of "non-qualifying goods" to which reference will be made (unhappily frequent amendments in statutes relating to fiscal matters are by no means unusual). In terms of section 5 of the Act sales tax was payable in respect *inter alia* of goods sold as well as imported into the Republic on or after 3 July 1978, subject to the provisions of Section 6. Section 6, in its turn, had to be read with Division 1 of schedule 2 to the Act and, in particular for present purposes, with the provisio to paragraph 3(b) thereof. For the purposes of this appeal the screen plates were, other than in two instances, purchased before 14 October 1987; the wires were all purchased before that date and the wet felts also all before that date. The date 14 October 1987 is relevant because items (3) and (4) of the list

of non-qualifying goods were amended with effect from that date.

It is not necessary to trace the many amendments in this respect and I quote in so far as relevant sections 6 and Schedule 2.

Section 6 provided:

> "6(1) The tax will not be payable in respect of any taxable value which, but for the provisions of this section, would be determinable in respect of the following, namely-
>
> (a) .....
>
> (b) .....
>
> (c)(i) subject to compliance with the provisions of section 14, sales of goods or taxable services rendered to a vendor who is registered under section 12 in respect of an enterprise falling within a category of enterprises mentioned in Schedule 2, if such goods or services are goods or services described in that Schedule in relation to such category and are intended for use or utilization in such enterprise.
>
> (ii) .....
>
> (d) ....."

Schedule 2 to the Act provided, as a result of Act 99 of 1984 and prior to the amendment thereof by Act 86 of 1987:

"SCHEDULE 2

(SECTION 6 OF THIS ACT)

Exemptions: Certain sales of goods and taxable services

The categories of enterprises and the goods and taxable services in respect of which the exemptions applicable under the provisions of section 6(1)(c), (t) and (v) shall apply, shall be as hereinafter set forth.

DIVISION 1

Manufacturing Enterprises

In the case of any enterprise in the ordinary course of which goods (other than goods in respect of which an exemption under section 6(1)(d) applies) are manufactured or assembled for sale or any process of manufacture is undertaken for reward, the goods and taxable services set forth in this Division .....:

1. .....

2. .....

3.(a) Any repair or maintenance service-

(i) in respect of machinery or plant used directly in the manufacture, assembly or processing of

goods for reward or for sale; or

(ii) .....

and parts and materials purchased by the vendor carrying on the enterprise concerned for incorporation in or attachment to such machinery or plant in order to have such service effected.

(b) Parts and materials purchased for incorporation in or attachment to such machinery or plant for the purpose of the repair or maintenance thereof by the vendor carrying on the enterprise concerned.

(c) .....

Provided that for the purposes of this paragraph, parts and materials purchased shall not include any goods described in this Division under the heading of non-qualifying goods.

4. .....

5. .....

6. .....

7. .....

Non-qualifying goods

(1) .....

(2) .....

(3) Tools, accessories or ancillary equipment attached to machinery or plant and which come into direct contact with goods which are being processed and which by their specific function alter such goods or are used for the purposes of

brushing, crushing, cutting, forming, honing, machining, mixing, moulding, painting, polishing or screening.

(4) Tools, accessories or ancillary equipment attached to machinery or plant used for the purpose of handling goods which are being processed.

(5) Greases and lubricants

(6) Cutting oils

(7) Filtering and screening materials

(8) Cleaners and disinfectants

(9) ....."

(This list contained at the time 19 items and it is unnecessary to quote further. Items 5 to 8 sufficiently indicate the manner in which particular materials or parts have been added or changed from time to time as also the manner in which specific goods and classes of goods have from time to time been included in the list.)

With regard to items (3) and (4), as they read after 14 October 1987, it will suffice to say that, by the amendments taking effect on that day, the words "or ancillary" in the first line of each item were deleted and the words "or component parts" were added after the word "equipment". (Section 21(1)(a) of Act 86 of 1987.)

Before undertaking the exercise of applying these provisions to the facts there is one further observation to be made regarding the Act. Section 23 of the Act was in the following terms:

> "23. The burden of proof that any amount is exempt from or not liable to the tax chargeable under this Act shall be upon the person claiming such exemption or non-liability, and upon the hearing of any appeal from any decision of the Secretary, the decision shall not be reversed or altered unless it is shown by the appellant that the decision is wrong."

What is fundamental to a tax appeal such as the present is that everything depends on the particular facts of the case. Counsel were agreed that no ascertainable design behind the Act and Schedule could be discerned and it seems to me that they are, in this respect, correct. While the overall purpose of the legislation - namely to raise revenue - is clear, the transactions which were, at any given time, to be levied with tax follow no regular pattern. No statutory purpose can thus be invoked as an aid to interpretation, particularly in so far as the list of non-

qualifying goods is concerned. The frequent amendments suggest nothing other than arbitrary fiscal decisions.

A preliminary observation seems to be called for. The respondent was and the Special Court and the court *a quo* were required to make findings which in my view may be made by the simple process of posing a series of logical questions in an orderly sequence. To illustrate. What must be ascertained in the initial enquiry (dealing with the terms of paragraph 3 (b) of the Schedule) would be: are all the items involved in each case "parts or materials"; (and if so), were they "purchased for the purpose of repairing or maintaining the plant"; (and, if so) were they incorporated in or attached to such plant.

Unlike the case of Mondi (to which I have made reference) no issue arose in this case regarding the meaning of the phrases "incorporation in" and "attachment to". In the Mondi case the question was whether the words "incorporation in" and "attachment to" indicated that a distinction was to be drawn between these two concepts. In the

present case counsel for the appellant, as I understood him, did not find any comfort in this proposition. It was accordingly common cause between the parties that the conditions of paragraph 3 (b) had been satisfied. I would add only that it seems clear that no rigid set of criteria can be applied in answering the questions I have suggested. The processes of manufacture must be so multifarious as to preclude the formulation of a restricted or limited set of criteria.

Counsel's argument, notwithstanding the concession that the requirements of paragraph 3(b) were satisfied, focused on the question of whether the requirement of "attachment to" the machinery was satisfied by questioning in each case whether the screen plates, wires and felts were "essential to the process" or "an integral part of the machine". "Essential" and "integral" are not words used in the schedule and are accordingly not independent characterising features. This is not to say that these concepts may never be useful or appropriate in deciding questions such as whether a given article is to be classified as "a part".

But once the conclusion has been reached that the item is "a part" no further enquiry as to its essentiality or as to whether it is integral is called for. The failure to perceive this fact pervades counsel's argument and it is in this respect therefore misconceived.

In my view the correct application of the list of non-qualifying goods must be that the approach suggested above again be adopted. The first question would be whether the particular item has the character of a tool, an accessory, an item of ancillary equipment or, (after 14 October 1987) a component part. The criteria here again cannot be rigidly prescribed. Common sense will dictate what in any given machine or plant will qualify under each of these descriptions. Nor in my view would it be a matter of concern if in a given case there was found to be a measure of overlap between the separate descriptions. One item could thus appropriately be described as either an accessory or as ancillary equipment. An example may serve to explain what I have in mind. Most cameras on sale and in use today are equipped to receive a range

of lenses of different focal lengths. Are such lenses to be described as accessories or as ancillary equipment? Either description will probably be adequate but circumstances may make the one or the other more appropriate.

It is for this reason too that very little guidance may be found in decisions in the Courts dealing with items of equipment other than those with which I am concerned or with other goods on the list of non-qualifying items. In this case frequent recourse was had by counsel for the appellant to the judgment of Corbett JA in the case of CIR v Dunlop South Africa Limited 1987 (2) SA 878 (A). The point can be appreciated if it is recognized that the Court was required to decide whether certain "bladders" (used in tyre making) constituted parts purchased for incorporation in or attachment to curing machines and whether the bladders constituted either detachable machines tools or cutting, forming, honing or moulding tools. These were questions to be decided on the evidence given in that case and in relation to the

particular plant and machines involved and the wording of the Schedule then current. It was in this context that the Court discussed the words "machine tool". While certain of the criteria discussed may also be of application in the present case it does not follow that any one such criterion necessarily must be suitable to the present case. Mr Derksen's insistence that, for example, the nature of a "tool" had by that judgment been decided for all purposes is misplaced. All that was decided was what the criteria appropriate to that case were and how they were to be applied.

With that description of the manner or the process by which the legislation is to be applied I turn to consider, in relation to each of the items of equipment, the remaining questions which arise to determine whether or not the items are to be characterised as falling within the list of non-qualifying goods.

Firstly the screen plates. These are large items of equipment which on the evidence are attached by bolts to a part of the plant known

as a vibrating trough with the object of eliminating certain impurities or coarser materials (known as contraries) from the pulp slurry in the course of converting the slurry, in conjunction with a number of other processes, into paper. The screen plates are subject to wear and are made to be replaceable - on a average of once a year. This process takes approximately 9 hours per plate to complete. The screen plates are also designed in various configurations to remove different sizes or degrees of impurities according to the type of paper to be produced.

There cannot be any argument but that they are attached to the machinery; nor that they both came into direct contact with the goods (the slurries) being processed and by their specific function altered the goods. They would therefore fall into the category of non-qualifying goods in item (3) and not be exempt from tax if they were (also) tools, accessories or ancillary equipment.

The Special Court dealt with screen plates on the basis that they were covered by item (7) of the list of non-qualifying goods - namely

"Filter and Screening materials". The Court below held this not to be the case. I am of the same view as the Court below because the plates are not in this context "materials", they are "parts". It further held that the screens were covered by item (3) of the list. Counsel's argument in this Court was that the screens are not tools (as was held by the Court below) or accessories or ancillary equipment. The finding of the Court below that they were tools is founded upon the wide dictionary meaning of the word. I consider that there may well be contexts in which, in the process under consideration, one could refer to the screens as being the tools in the process which effect the screening of the slurry but this is perhaps somewhat contrived. For the purposes of this judgment it is unnecessary to debate this proposition because it is clear that the screens are both accessories and ancillary equipment in the same sense as the camera example given above.

Counsel's further argument based upon questions as to whether the screens could be regarded as "separate functional units"; or were

"integral" or had (or did not have) "some measure of separate existence and function" all appear to me to be either unhelpful or beside the point for the reasons already given.

As far as the screen plates are concerned it is also necessary to consider the position after 14 October 1987 because of the amendment affected by Section 21(1)(a) of the Taxation Laws Amendment Act 86 of 1987. In my view the addition of the words "or component parts" can only serve to further underline the finding to which I have come. I can see no reason why the screens may not also be characterised as "component parts". None of the terms used are used in a mutually exclusive sense and counsel's argument has failed to persuade me otherwise.

All the transactions involving screens were therefore rightly held by the commissioner to be liable to tax. It is not necessary to discuss Section 23 - the case is even clearer that the provisions that section would demand.

Next I consider the wet felts. Here the matter may be dealt with more briefly as counsel's arguments took, in essence, the same form as with the screens - that is to say the argument was confined to the question of whether the felts were covered by the non-qualifying list. The argument was again directed to concepts such as what constitutes a "tool" and whether as tools the felts could be said to be "attached to the machinery" because (so it was argued) the felts formed an "integral", "essential" or substantial" part of the machinery. The argument included again references to the Dunlop case (*supra*). What I have said of these arguments above also applies here.

In the case of the felts, as with the screens they were regularly replaced and were interchangeable for the purpose of different grades of paper. The method was to fit them over the appropriate drying cylinders to perform a necessary function in relation to the drying process - that is to absorb water from the then partially processed slurry. It can scarcely be denied that they are attached to the machinery; that they

came into contact with the slurry being processed; and that they altered the slurry being processed.

The Special Court held that the wet felts did not qualify for exemption because they fell within item (3) of the non-qualifying list. The full court of the Cape Provincial Division confirmed this finding. I also hold that this is the case. Again this is not a finding which warrants a discussion of Section 23. It is an even clearer case.

Finally there are the wires. Here again it was common cause that the purchases of wires were transactions falling within the ambit of paragraph 3(b) of the Schedule. The wires, on the evidence, are used in conjunction with the formers found in the first section of the plant. The formers lie in a horizontal position and act in conjunction with the "couch rolls". The formers are cylinders which constitute a mould on which the paper is formed. They are made of a bronze material, have a multiplicity of holes through the shell and are fairly smooth. This is the feature which calls for the use of the wires. The wires fit over the shell

of the rollers. Depending on what grade or type of paper is being made different layers of wires are used (usually two it seems) and the wires are classified by the number of meshes per square inch (apparently imperial units are or were still used). They can be of either stainless steel or plastic. They are supplied in tube form and are pulled over the drum rolls. Their function is to dewater the pickup layer of the sheet of paper being formed. The thickness of the paper being formed is determined by the size of the mesh of the top wire, the speed at which the former rotates and the rate at which the pulp is fed. Where several layers are used they form, as it were, a unit.

So viewed the wires are again in my view either accessories or ancillary equipment. They are clearly attached to the machinery and they come into direct contact with the slurry which is being processed and by their specific function alter it. The Special Court held that the wires qualified for exemption. The full Court held that they did not. In my view the wires do fall within item (3) of the non-qualifying list. The

question of whether (as the full Court held) the wires were "tools" in the broad sense need not be discussed. For the reasons I have given the order by the full court was correct.

In the result the appellant has failed on each of the issues debated in this Court. It has not been argued that the costs order made in the Court below in so far as a distinction had to be drawn between the success achieved on the appeal and cross appeal should be varied. As far as the costs of this appeal is concerned they must follow the result.

The appeal is dismissed with costs including the costs of two counsel.

C PLEWMAN AJA

CONCUR:

BOTHA JA)
HEFER JA)
NESTADT JA)
HARMS JA)