C.A. No. 122214

NOVA SCOTIA COURT OF APPEAL
Cite as: Nova Scotia (Finance) v. Farmers Co-Operative Dairy, 1996 NSCA 84

Hallett, Jones and Chipman, JJ.A.

BETWEEN:

THE MINISTER OF FINANCE Appellant - and - FARMERS CO-OPERATIVE DAIRY Respondent	Leanne M. Rodwell Hayes for the Appellant David P.S. Farrar for the Respondent Appeal Heard: March 25, 1996 Judgment Delivered: March 29, 1996

THE COURT: Appeal dismissed per reasons for judgment of Hallett, J.A.; Jones and Chipman, JJ.A. concurring.

HALLETT, J.A.:

This is an appeal by the Minister of Finance from a decision of the Nova Scotia Utility and Review Board allowing an appeal by Farmers Co-Operative Dairy Limited from an assessment by the Provincial Tax Commission that it was liable for tax under the **Health Services Tax Act**, R.S.N.S. 1989, c. 198, on certain equipment which Farmers claim was exempt from tax pursuant to s. 12(1)(n) of the **Act**.

Farmers is a manufacturer of dairy products.

Under the rather complex **Act** the purchase of tangible personal property is taxable at varying rates unless exempt. Section 12(1)(n) (formerly s. 10(1)(h)) provides:

> "12(1) The following classes of tangible personal property are specifically exempted from the provisions of this Act:
>
> > (n) subject to regulations, machinery and apparatus and parts thereof which are to be used or which are used in the manufacture or production of goods for sale."

The words "manufacture or production" are defined in s. 2(e) (formerly s. 1(ca)) of the **Act** as follows:

> "In this Act,
>
> (e) "manufacture or production" means the transformation or conversion of raw or prepared material into a different state or form from that in which it originally existed as raw or prepared material but does not include production or processing."

The words of the definition "but does not include production or processing" are irrelevant to the issues on this appeal; those words are defined in s. 2(l) of the **Act** and relate to the equipment used in non-renewable resource enterprises.

The Board, in allowing Farmers appeal, held that equipment used to create refrigerated storage for the purpose of storing ice cream, cheese and butter products as well

as milk ready for delivery was exempt from tax.

The Board did not agree with Farmers that the equipment used to store unsold milk products that were returned to the plant by Farmers delivery trucks that service small stores qualified for the exemption.

In reaching its decision the Board purported to apply the decision of Freeman J.A in **Stora Forest Industries Ltd. v. Nova Scotia (Minister of Finance)** (1991), 105 N.S.R. (2d) 115 (C.A.).

In **Stora 1991**, Freeman J.A. on behalf of this Court, after reviewing several decisions of the Supreme Court of Nova Scotia, at both the trial and appellate court levels respecting the manufacturing exemption, stated as follows:

> "14. Once the materials have been completely converted to goods for sale, the plant's finished product, and are ready for "transportation out", s. 10(1)(h) no longer applies. "Goods for sale" means goods not only packaged for eventual sale to retailers, but packed in containers for sale to the plant's own customers, presumably distributors or other manufacturers. Finished product cannot be allowed to pile up at the end of the production line: handling and holding of the goods for sale is a necessary incident of manufacture or production prior to "transportation out".
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> 15. The language of s. 10(1)(h) and s. 1 (ca) as it applies to machinery and apparatus used in the actual manufacture or production -- between transportation in and transportation out -- is broad and nonrestrictive, particularly since the removal of the words "directly and exclusively" by the 1982 amendment. Cases decided since 1982 suggest the following as a simple test or guide applicable to the facts of the present case: is the machinery and apparatus in question reasonably essential to the manufacture or production of goods for sale? Perhaps that becomes clearer if stated in the negative: can the goods for sale be manufactured or produced without the step in the manufacturing process performed by the machinery or apparatus in question? The manufacturing step might previously have been performed by manpower or by some other process, but it must be shown to be reasonably necessary to the finished product."

In short, after considering the decided cases since 1982, this Court established

a test or guide that should be applied to the facts of any particular case where an exemption under s. 12(1)(n) is claimed.

Facts

There were four storage areas relevant to the exemption claimed by Farmers. In its decision the Board pointed out that the ice cream storage area is for ice cream that is delivered to that area after it is manufactured. The facts disclosed, as recognized by the Board, that when ice cream leaves the production area it is still soft and it must be in refrigerated storage for at least 24 hours before delivery to customers.

I have already made reference to the storage for returned milk.

The next item considered by the Board was the walk-in box used to store cheese and butter products after production and before delivery.

The fourth area considered by the Board was the milk storage area which is a large refrigerated storage room kept at 4 degrees celsius in which all milk and cream products are stored prior to delivery.

The evidence showed that the Department of Agriculture requires the maintenance of certain temperature and humidity levels in these storage areas.

After making reference to the decision in **Stora 1991** and a recent decision of the Board in **Clearwater Arctic Surf Clam Inc. v. The Provincial Tax Commission** (1994), Tx - 94 - 14 in which the Board concluded that Justice Freeman's comments in **Stora 1991** do not mean that all equipment used for storage is exempt, the Board reached the following conclusion on Farmers' appeal:

> "The Board finds that the refrigerated storage areas in the present case fall within the parameters of manufacturing equipment, that is, after 'transportation in' and before 'transportation out' which includes the holding of goods for sale. The refrigerated storage of the finished products produced by the Appellant is necessary to produce a saleable product.

> The Board does not include the storage of return milk amounting to three tons of production in the calculation of the exempt portion. The Board finds that once the goods are taken from refrigerated storage they are beyond the point of 'transportation out' as defined by Freeman, J.A."

The Board therefore reduced the assessment.

The Minister of Finance asserts on this appeal that the Board failed to apply the "reasonably essential test" that was enunciated by Freeman J.A. in **Stora 1991** to the facts and, therefore, the Board misinterpreted s. 12(1)(n) of the **Act**.

The appellant's argument is stated in its factum as follows:

> "16 a. The Act defines production as a change, transformation or conversion of material into a different state or form. No transformation or change occurs or is continued at the refrigerated storage stage. The milk is ready for delivery when it arrives at refrigerated storage; no additional "production" is required. Milk products reaching this stage are ready for sale, and could be sold right off the production line; they could be loaded directly onto trucks and delivered to retail stores or other customers. The Appellant submits that storage at the end of the production line is necessary to transportation-out but is not necessary to the production line. Once products have left production, the section 12(1)(n) exemption is no longer applicable.
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> b. Refrigerated storage at the plant does not differ from milk product refrigerated storage at retail stores. The Respondent's position and the decision of the Board lead to the conclusion that the same activity is tax-exempt at one location but taxable at another. The Appellant submits that there is no difference between these two activities, and would further submit that there is no difference between refrigerated milk storage after production and return milk storage, which was found to be taxable by the Board. The act of attempted delivery does not alter the nature or state of the milk products from the time they first arrived at the refrigerated storage area.
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> 17. The Appellant therefore submits that the answer to the question phrase in Stora is yes, the goods for sale can be manufactured or produced without the step in the manufacturing process performed by the machinery or apparatus in question. Further, the Appellant submits that the statement made by the Board at page six of the decision (page eight of the Appeal Book) as follows is incorrect: "The refrigerated storage of the finished

> products produced by the Appellant is necessary to **produce** a saleable product." While refrigerated storage is necessary to **maintain** a saleable product, at this stage production is complete. The Act does not contemplate an exemption for storage of finished goods for sale."

Counsel for Farmers asserts that the issue in this case is the determination of the point at which the manufacturing operations of the respondent have ceased. Counsel for Farmers asserts that the refrigeration equipment in question serves to further process the respondent's goods prior to sale and, in addition, that after production of the goods has been completed the goods must be stored in an appropriate manner to preserve them for sale. He relies, in part, on a decision of Kelly J. in **Continental Seafoods Limited v. Nova Scotia (Minister of Finance)** (1992), 112 N.S.R. (2d) 361, a case that dealt with the construction of refrigeration facilities as part of the production of certain fish products for the export market. The evidence in that case disclosed that the fish had to be processed in controlled temperature conditions in order to meet customer specifications. Kelly J. concluded that the use of cold rooms was clearly part of the process as it was necessary to use this equipment. That decision was overturned by the Appeal Court in a decision reported in (1993), 121 N.S.R. (2d) 176 but on other grounds.

Counsel for Farmers also relies on a decision of MacIntosh J. in **Northland Fisheries Limited v. Nova Scotia (Minister of Finance)** (1986), 77 N.S.R. (2d) 361 in which it was decided that refrigerated storage serves to prevent the transformation of a saleable product into an unsaleable product. In that case the equipment (insulated fish boxes) was used to prevent raw fish from spoilage. MacIntosh J. stated:

> "Where, as here, it is necessary to move the raw fish from one area to another, these insulated boxes are a necessary apparatus to ensure a saleable product will result. They are an integral part of the apparatus used to produce a saleable product. They are used to transform or convert fish into a different state from that in which it originally existed, i.e., from a perishable to a nonperishable state."

Counsel for Farmers also relies on a decision of Freeman J.A. in **Minister of Finance v. Farmers Co-Operative Dairy** (unreported, December 4th, 1995) where this Court held in a case involving the need for a dairy to have equipment to sanitize holding tanks for milk prior to processing stated:

> "Where manufacturing or production actually begins is a question of fact that can vary depending on the materials or the goods into which they are to be transformed. Milk is so highly perishable that a major object of the manufacturing process, of liquid milk at least, is to make it less perishable. Every step taken to further that objective is part of the process. Holding the milk in sanitized and insulated tanks is therefore essential to the process. It follows that equipment for sanitizing the tanks must be a necessary part of that process.
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> . . . . .
>
> The answer is obvious in the present circumstances: milk would not be fit for human consumption if not held in clean containers at every stage. Cleanliness is an essential part of the manufacturing or production process that must begin the moment the milk is received."

In short, counsel for Farmers argues that the products manufactured by Farmers would not be fit for human consumption if not held in the refrigeration areas prior to sale and, therefore, the refrigeration areas in the present case make the product less perishable. Therefore, the equipment used to refrigerate these storage areas is part of the production process and should be exempt pursuant to s. 12(1)(n) of the **Act**.

Disposition of the Appeal

An appeal to this Court is limited by s. 30 of the **Nova Scotia Public Utilities and Review Board Act**, R.S.N.S. 1992, c. 11 to questions of law or jurisdiction. Whether or not certain equipment qualifies for the exemption under s. 12(1)(n) is a question of fact

assuming the correct test is applied. Section 28 of the **Public Utilities and Review Board Act** provides that a finding of the Board upon a question of fact within its jurisdiction is binding and conclusive. This Court has reviewed decisions of the Board on this type of issue. I will consider the issue raised by the appellant but in the context of the limited jurisdiction of this Court to intervene.

In arriving at its decision the Board gave consideration to the transport-in/transport-out concept set out in paragraph 14 of the **Stora 1991** decision. However, what I would refer to in colloquial terms as, the bottom line of the Board's decision was that "the refrigerated storage of the finished products produced by [Farmers] is necessary to produce a saleable product". In effect, the Board applied the simple test described by Justice Freeman in paragraph 15 of the **Stora 1991** decision which I have previously set out in these reasons.

It would also appear that the Board must have given consideration to the decisions in the **Continental Seafoods** and **Northland Fisheries** cases which dealt with the necessity of using refrigerated equipment when processing perishable products.

In my opinion when considering the manufacturing and production equipment exemption with respect to perishable products the words "goods for sale" as contained in s. 12(1)(n) of the **Act**, by necessary implication, must mean goods for sale in a saleable condition. Storage of perishable products in refrigerated storage is usually essential to the production of saleable goods. The argument of the appellant that such storage is not for the purpose of producing goods for sale but merely for the purpose of maintaining a saleable product is far too neat a distinction to draw and is contrary to the case law relating to refrigerated storage equipment (**Continental Seafoods** and **Northland Fisheries**).

The appellant's analogy that refrigerated storage at Farmers plant does not differ from refrigerated storage for milk products in retail stores which are not exempt from a tax under the **Act** is not sound; the retail store is not a manufacturer or a producer of goods for

sale.

The refrigeration equipment at Farmers plant makes the products less perishable which is essential to the production of a saleable product by a manufacturer.

I agree with the comments of the Board in the **Clearwater** case that Freeman J.A.'s comments do not mean that all storage facilities are exempt under s. 12(1)(n). Whether the exemption applies depends on the purpose and use of the tangible personal property in question. The statement of Justice Freeman in paragraph 14 of **Stora 1991** decision that finished products cannot be allowed to pile up at the end of the production line and that the handling and holding of the goods

for sale is a necessary incident of manufacture or production prior to transportation out must be viewed in the light of the test which he developed in paragraph 15 of that decision. That test is workable and it would seem to me that is the test that should be applied by the Commission and the Board when considering whether or not equipment is covered by the exemption provided for in s. 12(1)(n) of the **Act**.

Conclusion

In my opinion, the Board directed its mind to the key question before it; that is whether the refrigerated storage equipment in question was reasonably necessary to produce a saleable product. In answering this question Commissioner Skinner, who has had considerable experience in dealing with these issues, appears to have applied the test enunciated by Freeman J.A. in **Stora 1991**. Therefore, the Board did not misinterpret s. 12(1)(n) and, thus, did not err in law. Whether a piece of equipment qualifies for s. 12(1)(n) exemption is essentially a question of fact for the Board assuming it applies "the reasonably essential test". The Legislature has directed that there is no appeal to this Court on such an issue. Accordingly, the appeal ought to be dismissed with costs to Farmers in the amount of $1,000 plus disbursements.

Hallett, J.A.

Concurred in:

Jones, J.A.

Chipman, J.A.

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Appellant	)	
- and -	)	REASONS FOR JUDGMENT BY:
FARMERS CO-OPERATIVE DAIRY	)	HALLETT, J.A.
Respondent	)	