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Case No 202/1988

IN THE SUPREME COURT OF SOUTH AFRICA  
APPELLATE DIVISION

In the matter between:

NATIONAL CO-OPERATIVE DAIRIES LIMITED

Appellant

and

THE COMMISSIONER FOR INLAND REVENUE

Respondent

CORAM:

CORBETT CJ, VAN HEERDEN, NIENABER,  
VAN DEN HEEVER JJA et NICHOLAS AJA

HEARD:

5 NOVEMBER 1991

DELIVERED:

26 NOVEMBER 1991

JUDGMENT

VAN HEERDEN JA:

In each of its returns for the income tax years ending 30 June 1975 to 30 June 1982 the appellant sought to deduct certain items from its income. These were, however, disallowed by the respondent. In determining the tax payable by the appellant he accordingly added back the amounts in question. Consequent to the dismissal of an objection to this decision, the appellant appealed to the Transvaal Special Income Tax Court. That court disallowed the appeal. Subsequently the appellant obtained leave to appeal direct to this court.

The material facts are not in dispute. In setting them out I borrow freely from the concise summary in the judgment of the court a quo.

The appellant is a farmers' special co-operative company, registered under the Co-Operative Societies Act 29 of 1939. It conducts large-scale operations in the dairy industry. Part of its activities is to collect milk from a large number of

its members, being dairy farmers. That milk is conveyed to a number of depots. Approximately half of the milk is intended for use as drinking milk and half for processing into a variety of dairy products.

If milk is not cooled within four hours after it is extracted from the cow's udder, bacterial degeneration ensues. Cooling, however, materially delays such degeneration. Pasteurisation also delays degeneration and moreover kills all bacteria harmful to human life. This is a process whereby milk is heated for a short period to approximately 72°C and then cooled again.

Over the last decade or so the appellant has been utilising two types of equipment for combating an increase in the bacterial content of milk. The first is a cooling unit, a tank, which is provided by the appellant to a farmer under a contract of lease and installed in the latter's dairy. By various means, but principally through a milking machine, the farmer

causes the milk drawn from the udder to be transferred to the tank. The temperature of the fresh milk, 37°C, is there reduced to the ideal temperature for the preservation of milk, i e, between 3° and 5°C. Every second day the milk is collected from the farmer. To this end the appellant makes use of insulated tankers. The driver of the tanker tests the milk in the tank, and if it is acceptable it is pumped into the tanker where its temperature remains constant. This process is repeated at various other dairy farms. Eventually the milk so collected is conveyed in the tanker to one of the appellant's depots. There the contents of the tanker are pumped via a cooler into a storage silo. After treatment in the pasteurisation plant the milk is then either bottled for consumer use or sent to so-called industrial plants where it is processed into dairy products such as butter, cheese and condensed milk.

If a farmer does not make use of a cooling

tank, he follows the rather old-fashioned procedure of running the milk over a water cooler into cans, thereby reducing the temperature of the fresh milk from 37°C to the temperature of the water in the cooler - in the summer months in the vicinity of 20°C. The milk is then poured into cans which are collected by the appellant daily and transported to one of its depots by means of flat-bed trucks.

The amounts which the appellant sought to deduct from its income related to the cost of the tanks, tankers and trucks. In the Special Court the appellant contended that the deductions should have been allowed under s 12(1)(a) and 12(2)(a), alternatively under s 27(2)(d) and (e), of the Income Tax Act 58 of 1962. In this court, however, counsel for the appellant rightly conceded that the tanks did not qualify for the allowances provided for in these sections, but maintained that the tankers and trucks did so qualify.

I shall deal first with the provisions of

s 12(1)(a) and 12(2)(a). In so far as it is material,

s 12(1)(a) provides:

"12(1) In respect of -

(a) new or unused machinery or plant which is brought into use by any taxpayer for the purposes of his trade ... and is used by him directly in a process of manufacture carried on by him ....

there shall ... be allowed to be deducted from the income of such taxpayer for the year of assessment during which such machinery or plant is so brought into use an allowance, to be known as the 'machinery initial allowance' ...."

S 12(2)(a) makes provision for the deduction of a "machinery investment allowance" in respect of new or unused machinery or plant provided, inter alia, that it is used by the taxpayer "directly in a process of manufacture carried on by him".

It was common cause that the deductions claimed by the appellant in respect of the cost of the tankers and trucks qualified under s 12(1)(a) and s 12(2)(a) if they were used by the appellant directly in a process of manufacture carried on by it. It was

contended by the appellant, and conceded by the respondent, that the pasteurisation of milk by the appellant constitutes a process of manufacture, and I shall assume that the concession was rightly made. On this assumption the cardinal question is whether the tankers and trucks are used by the appellant directly in the process of pasteurisation. The answer depends on the solution of a further question, viz, at what point does that process begin?

Counsel for the appellant sought to establish a link between the cooling of the milk in the tanks and the eventual pasteurisation. His contention was that the process of manufacture commenced with the feeding of the milk into the tank. The cooled milk, so he submitted, is something essentially different from the fresh or raw milk extracted from the udder. This is not borne out by the evidence. The only purpose of the cooling of milk is to preserve it, i e, to inhibit bacterial growth. Cooling does not change the

substance or chemical composition of fresh milk. Indeed, save for a change in temperature, there is no difference at all between fresh and cooled milk. Hence there is no question of the milk being subjected to a series of operations, beginning with the cooling thereof, which as a whole change the substance of the raw product. This is borne out by the fact that milk not cooled in a tank can be pasteurised, as happens with milk collected in cans. In the final analysis there is no difference between the cooling of milk in a tank and the cooling thereof in a refrigerator. And the housewife who put a jug of fresh milk in a refrigerator with the intention of preserving it for later use as an ingredient in the baking of custard would surely be surprised to hear that the baking commenced when she closed the door of the refrigerator.

In the alternative counsel for the appellant submitted that the tankers and trucks are in any event used in the process of pasteurisation because they are



utilised to convey the milk to the depots where that process takes place. Whilst it is true that without such conveyance pasteurisation cannot take place, the tanks and trucks are clearly not used directly in a process of manufacture (pasteurisation). That process does not begin until, at the soonest, the raw product - the milk - reaches the depot.

I turn to the provisions of s 27(2)(d) and (e) of the Act. In so far as it is material s 27(2)(d) reads:

"(2) In the determination of the taxable income of any agricultural co-operative, there shall be allowed as deductions from the income of such ... co-operative ... -

(d) (i) an allowance, to be known as the special machinery initial allowance, in respect of the cost to such agricultural co-operative of any new or unused machinery or plant which ... is used by it directly for storing ... pastoral, agricultural or other farm products of its members ... or for subjecting such products to a primary process ..." (My underlining.)

It is unnecessary to set out the provisions of s 27(2)(e). It suffices to say that if plant or machinery does not comply with the above underlined requirements no allowance may be claimed under s 27(2)(e). It follows that the appellant's tankers and trucks do not fall within the ambit of s 27(1)(d) and (e) unless i) they are used directly for storing its members' milk, or ii) are so used for subjecting such milk to a primary process.

Counsel for the respondent contended that these requirements are not met for the simple reason that the appellant becomes the owner of the milk when it takes delivery thereof from the farmer. I find it unnecessary to consider this submission and shall assume, in favour of the appellant, that the milk conveyed in and on the tankers and trucks is to be regarded as "products" of its members.

On behalf of the appellant it was submitted, albeit faintly, that the tankers - but not the trucks -

are used for storing milk. There is no merit in this submission. The ordinary meaning of "store" is to keep in store in reserve or for future use (cf the word "op-berg" in the Afrikaans text). By contrast the tankers are used for the conveyance of milk and there is simply no question of a use for storage whilst the milk is in transit from a dairy to one of the appellant's depots.

The final argument of the appellant was that the tankers and trucks are used for subjecting the milk to "a primary process". That concept is defined in s 27(d). Applied to the facts of this appeal it is the first process to which milk is subjected by the appellant in order to render it marketable or to convert it into a marketable commodity. If the cooling of milk in a tank can be regarded as such a first process it is, of course, the farmer and not the appellant who subjects the milk to that process, even although some guidance is afforded to him by the appellant. The tankers collect the milk after it has

been cooled. No further cooling takes place whilst the milk is in transit. Nothing further is done during the process of conveyance to render the milk marketable or to convert it into a marketable product. Nor are the tankers - and the trucks - used directly in a primary process to which the milk may be subjected after it is fed into a silo. The connection between the use of the tankers - and obviously also the trucks - and the eventual process is simply too tenuous to qualify as a direct use for the later primary process.

The appeal is dismissed with costs, including the costs occasioned by the appellant's application for condonation of the late filing of the record which, not being opposed, was granted at the hearing of the appeal.



H J O VAN HEERDEN JA

CORBETT CJ

NIENABER JA

VAN DEN HEEVER JA

NICHOLAS AJA

CONCUR