


# ***STD 2000/2 - Sales tax: classification of absorbent stone and clay granules***

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# Sales Tax Determination

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## Sales tax: classification of absorbent stone and clay granules

### *Preamble*

*This document is a ruling for the purposes of section 77 of the **Sales Tax Assessment Act 1992** and may be relied upon by any person to whom it applies.*

### **Background**

1. This Determination sets out the Australian Taxation Office (ATO) view on the sales tax classification of absorbent granules that result from the quarrying, drying and crushing of certain stones and clays. It also considers the implications of the decision in *IGY Manufacturing Pty Ltd v. FC of T* 99 ATC 4860; (1999) 42 ATR 544 for the general classification of goods under Item 40 in Schedule 1 to the *Sales Tax (Exemptions and Classifications) Act 1992* (ST(E&C) Act).

2. In *IGY Manufacturing*, the Federal Court (Hely J) decided that absorbent granules (marketed under the name 'Dri-Cat'), which resulted from the quarrying, drying and crushing of spongolite and kaolinite sedimentary rocks, were exempt from sales tax under subitems 40(1) and (2) as 'stone' and 'clay'. The 'Dri-Cat' product had a number of uses, including use as a pet litter to absorb waste and reduce odours and use to absorb industrial and commercial liquid spills.

### **Issues**

3. Are absorbent granules resulting from the quarrying, drying and crushing of stone and clay exempt from sales tax under Item 40 in Schedule 1 to the ST(E&C) Act?
4. How does the decision in *IGY Manufacturing* affect existing ATO policy on the classification of goods covered by Item 40?

### **Decision**

5. Where each of the following conditions is satisfied, absorbent granules are exempt from sales tax under Item 40 in Schedule 1 to the ST(E&C) Act:

- stone or clay is quarried, dried and crushed to form absorbent granules;
- no other ingredients are added in the course of processing the stone or clay;

- there has not been any significant change in the nature and physical characteristics of the stone or clay; and
- the absorbent granules are marketed for applications that rely on the nature and physical characteristics of the stone or clay from which they are formed.

6. The decision in *IGY Manufacturing* turned on its particular facts, and is not seen as having general application in relation to other categories of goods made from stone or clay or from any other material listed in Item 40 in Schedule 1 to the ST(E&C)Act.

## Reasons

7. The Commissioner's guide to the classification of goods is set out in Taxation Ruling SST 11: Sales tax: a guide to the classification of goods under the sales tax law. In order to classify goods for sales tax purposes, it is necessary to make an objective identification of the goods. One way to do this is to determine their essential character. This process generally involves deciding what is the basic nature of the goods and considering what the goods are made of and what they might be used for. However, as goods covered by Item 40 are considered to be **always exempt goods** for the purposes of the sales tax law, classification under Item 40 does not involve considering who actually uses the goods or how they are actually used.

8. In *IGY Manufacturing*, the ATO submitted that the process to which the stone or clay was subjected 'created a commercially different end product' from the stone and clay from which the material was originally derived, and that Item 40 was not intended to apply to such commercially different products because their essential character was not that of 'stone' or 'clay'.

9. Hely J, 99 ATC 4860 at 4866; (1999) 42 ATR 544 at 550 noted the potential for the application of that test, but considered the real question to be:

'... whether it is no longer appropriate to characterise the end product as stone. That question is answered by reference to a consideration of the nature and physical characteristics of the end product, rather than the uses to which it can be put, although a change in the available range of uses may not be entirely irrelevant to the characterisation question.'

10. In deciding that both before and after processing, the materials could be characterised as stone or clay, Hely J had regard to two aspects of the evidence. Firstly, the only way the material could be marketed for its absorbent properties was in its processed form; and secondly, that the processing involved no significant change in the nature and physical characteristics of the material.

11. It was also relevant that there were no other ingredients added in the course of processing the quarried stone and clay.

12. On the basis of the particular facts in this case, the ATO decided not to lodge an appeal against the decision.

**Interpretation of Item 40**

13. For the purposes of subsection 13(1) of the *Acts Interpretation Act 1901* (AIA), Schedule 1 to the ST(E&C) Act is deemed to be a part of that Act (see subsection 13(2)). Subsection 13(1) deems the headings of the Parts and Divisions and, by inference, Chapters to be part of the ST(E&C) Act, and thus part of Schedule 1. Court decisions indicate that headings to Parts, etc. of an Act may be used to help in the interpretation of a provision in that Part, etc. While those decisions are not unanimous in their views of how a heading can be used as an aid in interpretation, largely reflecting the different statutory contexts in which the courts have considered the issue, it is the Commissioner's view that the interpretation of Item 40 should be seen in the context that it appears in Chapter 2 of Schedule 1, headed 'Building materials', and is surrounded by other Items that deal with a range of building materials.

14. It is noted that Hely J in *IGY Manufacturing* did not consider the interpretation of Item 40 in the context in which it appears in Chapter 2 of Schedule 1. Accordingly, the Commissioner considers that *IGY Manufacturing* has limited application to the interpretation of Item 40 outside of the particular facts in that case.

15. The context in which an Item appears was considered in *K Mart Australia Ltd v. FC of T* 96 ATC 4155 at 4161; (1996) 31 ATR 524 at 531. The Full Federal Court commented that:

'... the collocation or context can affect the meaning of a term and give it a connotation different to that which might otherwise be attributed if the term appeared in isolation.'

16. The context in which Item 40 appears, being collocated with Items exempting other goods used in building applications, and appearing in a Chapter headed 'Building materials', suggests that the goods covered by the Item must be able to be objectively characterised as stone, gravel, etc. that have a use as building materials. A similar approach is taken to the interpretation of Item 42 in Chapter 2 of Taxation Ruling SST 5: Sales Tax: classification of furniture, timber and joinery.

17. It has been suggested that goods such as precious stones, specifically covered by Item 3 in Schedule 5 to the ST(E&C) Act, could now also be covered by subitem 40(1) as a consequence of *IGY Manufacturing*. However, since subitem 3(2) in Schedule 5 refers specifically to precious stones, it prevails over a more general potential exemption provision. The specific provision is considered to reflect the clear intention of Parliament.

18. This view of the classification of goods potentially covered by more than one Schedule has judicial support in *Reece Pty Ltd v. FC of T* 97 ATC 5005 at 5009; (1997) 37 ATR 197 at 202. In that case, Harper J said:

'I also accept that I am required to keep clear of sales tax those goods which are described in the "exempting" Schedules, even if such goods are also described in the "taxing" Schedules. But these principles can not stand in the way of a taxing Schedule which clearly and with particularity includes the goods in question while, by contrast, the item in the Schedule said to be the source of the exemption refers to them – if it refers to them at all – by broad and inappropriate (rather than particular and apt) description.'

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## Commissioner of Taxation

19 January 2000

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*Previous draft:*

Not previously issued in draft form.

*Related Rulings/Determinations:*

SST 5; SST 11

*Subject references:*

absorbent granules; classification; mining and quarrying; sales tax; stone and clay

*Legislative references:*

- AIA 13(1)
- AIA 13(2)
- ST(E&C)A Subitem 40(1) Sch 1
- ST(E&C)A Subitem 40(2) Sch 1
- ST(E&C)A Item 65 Sch 1
- ST(E&C)A Item 3 Sch 5
- ST(E&C)A Subitem 3(2) Sch 5

*Case references:*

- IGY Manufacturing Pty Ltd v. FC of T 99 ATC 4860; (1999) 42 ATR 544
- K Mart Australia Ltd v. FC of T 96 ATC 4155; (1996) 31 ATR 524
- Reece Pty Ltd v. FC of T 97 ATC 5005; (1997) 37 ATR 197

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