



Ottawa, Thursday, March 31, 1994

Appeal No. AP-93-016

IN THE MATTER OF an appeal heard on September 15 and 16, 1993, under section 81.19 of the *Excise Tax Act*, R.S.C. 1985, c. E-15;

AND IN THE MATTER OF two decisions of the Minister of National Revenue dated March 31, 1993, with respect to a notice of objection served under section 81.15 of the *Excise Tax Act*.

BETWEEN

THERM-O-COMFORT CO. LTD.

Appellant

AND

THE MINISTER OF NATIONAL REVENUE

Respondent

DECISION OF THE TRIBUNAL

The appeal is allowed in part.

Kathleen E. Macmillan
Kathleen E. Macmillan
Presiding Member

Arthur B. Trudeau
Arthur B. Trudeau
Member

Lise Bergeron
Lise Bergeron
Member

Nicole Pelletier
Nicole Pelletier
Acting Secretary

UNOFFICIAL SUMMARY

Appeal No. AP-93-016

THERM-O-COMFORT CO. LTD.

Appellant

and

THE MINISTER OF NATIONAL REVENUE

Respondent

This is an appeal under section 81.19 of the Excise Tax Act of two assessments of the Minister of National Revenue. There are two issues in this appeal. The first issue is whether the appellant's hydramulch product, known under the tradename "Fibramulch," is exempt from sales tax either because it is a fertilizer or a pest control product and, therefore, falls within the provisions of Part IV of Schedule III to the Excise Tax Act. The second issue concerns certain sales of cellulose insulation and whether the property in the insulation that was sold passed to the purchasers prior to July 1, 1985. If property in the goods did pass before that date, the sales are not subject to sales tax.

HELD: *The appeal is allowed in part. With respect to Fibramulch as a fertilizer, the Tribunal accepts that Fibramulch does contain the three essential elements commonly found in fertilizers; however, because the quantities of those elements are so small and because the manner in which Fibramulch is applied severely limits the quantity of nutrients released, the Tribunal is not prepared to conclude that Fibramulch is a fertilizer. Regarding Fibramulch as a pest control product, the Tribunal is of the view that the applicable legislation contemplates preparations which are created specifically for the purpose of pest control. The intended purpose of Fibramulch is as a medium for growing grass, not as a pest control product. The fact that, in serving its intended purpose, it also conceals seeds from birds is not sufficient, in the Tribunal's opinion, to qualify it as a preparation for pest control purposes.*

With respect to some of the cellulose insulation transactions, property in the goods passed before the date that sales tax on those goods became exigible. The appeal is allowed in respect of these transactions. Regarding the balance of the cellulose insulation transactions, the Tribunal concludes that property passed after the relevant date and that, accordingly, sales tax is exigible.

*Place of Hearing: Ottawa, Ontario
Dates of Hearing: September 15 and 16, 1993
Date of Decision: March 31, 1994*

*Tribunal Members: Kathleen E. Macmillan, Presiding Member
Arthur B. Trudeau, Member
Lise Bergeron, Member*

Counsel for the Tribunal: John L. Syme

Clerk of the Tribunal: Janet Rumball

*Appearances: Bernard Wiley, for the appellant
Anne M. Turley, for the respondent*

Appeal No. AP-93-016

THERM-O-COMFORT CO. LTD.

Appellant

and

THE MINISTER OF NATIONAL REVENUE

Respondent

TRIBUNAL: KATHLEEN E. MACMILLAN, Presiding Member
ARTHUR B. TRUDEAU, Member
LISE BERGERON, Member

REASONS FOR DECISION

This is an appeal under section 81.19 of the *Excise Tax Act*¹ (the Act) of two assessments. Notice of assessment No. SWO 6842 was confirmed and notice of assessment No. SWO 6841 was varied by decisions of the Minister of National Revenue.

During the relevant period, the appellant manufactured cellulose insulation and a product referred to generically as "hydramulch" in the grass- or sod-growing trade. Shredded newsprint is the primary ingredient in both products.

There are two issues in this appeal. The first is whether the appellant's hydramulch product, known under the tradename "Fibramulch," is exempt from sales tax either because it is a fertilizer or a pest control preparation and, therefore, falls within the provisions of Part IV of Schedule III to the Act. The second issue concerns certain sales of cellulose insulation and whether the property in the insulation that was sold passed to the purchasers prior to July 1, 1985. If property in the goods did pass before that date, the sales are not subject to sales tax.

Sections 50 and 51 of the Act and Schedule III to the Act are relevant to this appeal. They, in part, provide:

50. (1) There shall be imposed, levied and collected a consumption or sales tax at the rate prescribed in subsection (1.1) on the sale price or on the volume sold of all goods

(a) produced or manufactured in Canada

(i) payable, in any case other than a case mentioned in subparagraph (ii) or (iii), by the producer or manufacturer at the time when the goods are delivered to the purchaser or at the time when the property in the goods passes, whichever is the earlier.

51. (1) The tax imposed by section 50 does not apply to the sale or importation of the goods mentioned in Schedule III.

1. R.S.C. 1985, c. E-15.

SCHEDULE III

PART IV

FARM AND FOREST

9. Fertilizers and materials for use exclusively in the manufacture thereof.

18. Peat moss when used for agricultural purposes, including poultry litter.

19. Preparations, chemicals or poisons for pest control purposes in agriculture or horticulture, and materials used in the manufacture thereof.

Mr. Bernard Wiley, President of Therm-O-Comfort Co. Ltd., testified on behalf of the appellant and acted as its representative.

With respect to the first issue, Mr. Wiley contended that Fibramulch should be exempt from sales tax on the ground that it is a fertilizer and/or a pest control preparation. He also called two witnesses, Mr. Bill Aimers, owner of The Grass Company Ltd., and Mr. Paul T. Flood, an environmental engineer employed by Paragon Engineering Limited.

The witnesses appearing on behalf of the appellant testified as to the use and properties of Fibramulch. They explained that the product is designed and used as a medium for growing grass. It is particularly well-suited for establishing grass on slopes and other difficult ground areas that are inaccessible to heavy machinery and, therefore, unsuitable for more traditional methods of growing grass. It is frequently used on golf courses, for example.

Fibramulch is shredded, recycled newsprint that has been dyed green. It is mixed with grass seed, then moistened and sprayed onto the soil. Fibramulch is not usually worked into the earth or used in combination with conventional fertilizers. Initially, the grass seed germinates in the mulch mixture. Later, as the mulch begins to break down, germinated seed establishes roots in the underlying soil.

According to witnesses for the appellant, Fibramulch is an excellent medium for growing grass. Its green colour conceals seeds from predatory birds, which are a real danger to the establishment of grass. Its thick mat prevents the growth of weeds. Moreover, its stable nature enables it to slowly release its nutrients into the developing grass when they are most required. In order to determine how much nourishment Fibramulch delivers in addition to percentage nutrient concentrations, loading rates and nutrient loss must be considered.

With respect to loading rates, witnesses for the appellant indicated that, notwithstanding the low concentrations of essential nutrients in Fibramulch, a grass grower can provide the seed with sufficient nutrients for a healthy crop by increasing the absolute amount of mulch employed. Regarding nutrient loss, Mr. Flood testified that the nutrients in conventional fertilizers such as urea can be quickly depleted if the fertilizer, once applied, is exposed to direct sunlight or rainfall. By contrast, Fibramulch is chemically stable and, thus, breaks down over an extended period of time. As a result, the nutrients in Fibramulch are not lost and are able to supply nourishment over the entire germination period and longer. Mr. Flood acknowledged that Fibramulch contains small quantities of nitrogen and virtually no potassium or phosphorous, the essential elements in fertilizer. However, after adjustments for differences in load rates and nutrient depletion, the nutrients supplied by Fibramulch could be comparable to those supplied by a urea fertilizer.

Regarding the issue of Fibramulch, counsel for the respondent called as witnesses Mr. Brian Radey, a fertilizer evaluation officer with the Department of Agriculture, and Mr. Keith Matthie, National Coordinator, Crop Protection, Canadian Horticultural Council, and a commercial farmer.

In the opinion of both witnesses, Fibramulch would never be used as a replacement for fertilizer because of its low concentration of nutrients.² Nitrogen, potassium and phosphorous are contained in many natural materials that are not sold as fertilizer. The witnesses acknowledged that urea and other common fertilizers could dissipate after application, due to exposure to sunlight and rainfall. However, they maintained that the dissipation rate was difficult to calculate and would be low if the fertilizer was used properly, i.e. incorporated into the soil. It was agreed that Fibramulch had certain features in common with peat moss. Both are natural materials that serve to increase the water retention of the soil.

Mr. Radey testified that, to be effective, animal and vegetable fertilizers have to be incorporated into the soil to permit microbes in the soil to interact with the organic matter in the fertilizer. He testified that, because Fibramulch is applied to the surface of the soil, the necessary microbial interaction and resultant release of plant nutrients will not occur.

The appellant's representative argued that the definitions of "fertilizer" and "control product" contained, respectively, in the *Fertilizers Act*³ and *Pest Control Products Act*⁴ do not bind the Tribunal. He submitted that the appellant's witnesses clearly established the value of the product in issue as both a fertilizer and a pest control. Mr. Wiley urged the Tribunal to reject a narrow interpretation of the legislation that would restrict the exemptions only to chemical products. He submitted that the benefit of any ambiguity should go to the taxpayer. Fibramulch, he maintained, is a recycled material that delivers the benefits of traditional fertilizer and pest and weed control products with virtually no environmentally damaging side effects.

Counsel for the respondent argued that, in the absence of definitions of "fertilizer" and "pest control" in the Act, the Tribunal is entitled to look at the common industry meaning of these terms and at definitions contained in other acts. In counsel's submission, the common industry meaning, which parallels the definitions contained in the *Fertilizers Act* and the *Pest Control Products Act*, suggests that the products should be manufactured or represented as fertilizers or pest control products. According to counsel, the evidence established that Fibramulch is not sold or represented as either. Simply because the product contains nutrients, it does not automatically qualify as a fertilizer since virtually all vegetable matter contains elements present in fertilizers.

Counsel for the respondent also argued that Fibramulch does not qualify as a pest control product. The product operates by disguising or camouflaging seeds, not by controlling pests. Taking the appellant's argument to the extreme, counsel argued, would mean that even ground covers such as tarpaulins would qualify as pest control products.

2. An analysis performed for the appellant and put into evidence revealed that hydramulch contains 0.17 percent nitrogen, 0.05 percent phosphorous and 0.05 percent potassium. By contrast, urea fertilizer typically contains 46 percent nitrogen and significantly higher levels of phosphorous and potassium than Fibramulch.

3. R.S.C. 1985, c. F-10.

4. R.S.C. 1985, c. P-9.

With respect to the second issue, Mr. Wiley provided testimony on the relevant sales of cellulose insulation. The federal government's May 1985 budget made sales of insulation subject to tax, effective July 1, 1985. Mr. Wiley testified that officials of the Department of National Revenue advised him that any insulation ordered by customers and invoiced before July 1, 1985, would not be taxable even if delivery occurred afterwards.

Approximately 20 sales of cellulose insulation are at issue in this appeal. Mr. Wiley testified that, with respect to each of those sales, the customer placed its order sometime before June 30, 1985. The invoices in respect of the sales all predate July 1, 1985.

Mr. Wiley explained the appellant's method of operation as follows. After receiving an order, the appropriate number of bags of insulation were placed in a trailer stored on the appellant's premises. At that time, the customer was invoiced and the invoice number was recorded on the appropriate trailer sheet to indicate that a certain number of bags in the trailer had been allotted to a customer. The appellant would subsequently deliver the insulation to the customer upon the customer's request. In the present case, in all but two instances, the insulation was delivered after June 30, 1985. In all instances, payment was received after that date.

Mr. Wiley drew the Tribunal's attention to invoice No. 15930 dated May 1, 1985, and invoice No. 16268 dated June 29, 1985. Invoice No. 15930 is in respect of 1,073 bags of insulation which were shipped to Park Lane Marketing (Park Lane) on consignment. Invoice No. 16268 is in respect of 504 of the 1,073 bags sent to Park Lane on consignment and 1,436 bags that had been previously shipped by the appellant to Park Lane. Apparently, the balance of the 1,073 bags provided to Park Lane on consignment had been sold by Park Lane by June 29, 1985.

When questioned on the provision on his invoices that read "All materials and equipment remain the property of Therm-O-Comfort Co. Ltd. until paid in full," Mr. Wiley maintained that such a provision is not legally enforceable and was not part of the appellant's dealings with its customers.

On the question of when property passed in the case of the insulation shipments, Mr. Wiley likened the appellant's situation to that of a car dealer who sells a specific car to a customer, but retains possession of the car and does not transfer it to the customer for two weeks. Like the car sold by the dealer, the insulation was earmarked for a particular customer and set aside. It was not available for sale to someone else. According to Mr. Wiley, in the customer's mind, property passed at the time the contract was made, not later when the goods were paid in full, notwithstanding the wording on the invoices. In his submission, the transfer of property is not dependent upon payment or delivery unless it is the expressed or implied intention of the parties.

Counsel for the respondent drew the Tribunal's attention to the provision on the invoices which states that property passes only after payment is made. Counsel submitted that, as payment occurred after July 1, 1985, all the transactions are taxable. Moreover, the goods in the trailer were not ascertained when the contract was formed. Counsel argued that for goods to be ascertained, they must be identified to a particular contract. Counsel submitted that, even though the trailer sheets indicated that a certain number of bags had been allocated to a customer, as the individual bags were not marked allocated, the goods were not identified to the contract. Even if they had been identified, however, the express condition governing passage of property ensured that, until payment was received by the appellant, which was sometime after June 30, 1985, no property would pass.

In determining whether Fibramulch would qualify for exemption from sales tax on the basis that it constitutes a fertilizer, the Tribunal relied on evidence regarding the product's use, its nutrient composition and its effectiveness relative to other commonly accepted fertilizers. In making its determination, the Tribunal did not consider itself bound by the definitions contained in the *Fertilizers Act*.

In the opinion of the witnesses testifying at the hearing, a fertilizer is something that provides nutrition to plants through some combination of nitrogen, potassium and phosphorus. It became obvious to the Tribunal, however, that there is a question of degree. Virtually all natural compounds contain some quantity of nitrogen and, yet, very few would be considered fertilizers. Mr. Flood acknowledged, for example, that straw contains a higher percentage of nitrogen than Fibramulch, but is not, in his opinion, a fertilizer. Moreover, Mr. Radey testified that, even if one accepts that there is some nutrient value in Fibramulch, in the absence of some interaction between the mulch and microbes in the soil, the nutrients would not be released.

The Tribunal accepts that a fertilizer's effectiveness depends not only on its nutrient value, but also on its rate of application and on climatic conditions at the time that it is applied. However, there was no evidence that Fibramulch is used in the quantities necessary to bring it within the effectiveness range of more commonly accepted fertilizers. In this regard, the Tribunal was persuaded by the evidence of Mr. Matthie, who argued that, if applied properly, the quantity of nutrients provided by urea and similar fertilizers would far surpass that of Fibramulch. The Tribunal accepts that Fibramulch does contain the three essential elements commonly found in fertilizers; however, because the quantities of those elements are so small and because the manner in which Fibramulch is applied severely limits the quantity of nutrients released, the Tribunal is not prepared to conclude that Fibramulch is a fertilizer.

In the Tribunal's judgment, the primary use and intended purpose of Fibramulch is as a medium for growing grass. That is how it is sold and used.

Another consideration is whether Fibramulch qualifies for exemption from sales tax on the basis that it is a pest control product. It is clear that Fibramulch is not a chemical or a poison. Nor does it, in the Tribunal's opinion, qualify as a preparation for pest control purposes. In the Tribunal's view, section 19 of Part IV of Schedule III to the Act contemplates preparations which are created specifically for the purpose of pest control. The intended purpose of Fibramulch is as a medium for growing grass, not as a pest control product. The fact that, in serving its intended purpose, it also conceals seeds from birds is not sufficient, in the Tribunal's opinion, to qualify it as a preparation for pest control purposes.

Briefly, Mr. Wiley raised the question of considering Fibramulch as peat moss. The Oxford English Dictionary defines "peat" as "[v]egetable matter decomposed by water and partially carbonized by chemical change, often forming bogs or 'mosses' of large extent.⁵" Simply put, the Tribunal is of the view that shredded newsprint dyed green does not fit within any accepted definition of peat moss. The goods in issue are not peat moss and, therefore, do not qualify under the exempting provision for peat moss.

5. Vol. XI, 2nd ed. (Oxford: Clarendon Press, 1989) at 405. A number of dictionaries contain similar definitions. For example, see the definition of "peat moss" in the Gage Canadian Dictionary (Toronto: Gage Publishing, 1983) at 833 or Webster's New Twentieth Century Dictionary of the English Language Unabridged, 2nd ed. (New York: Simon & Schuster, 1979) at 1319.

The second issue to be determined is whether the appellant is liable to pay sales tax in respect of the sales of cellulose insulation discussed herein. Subparagraph 50(1)(a)(i) of the Act provides that sales tax, which became leviable on the goods in issue on July 1, 1985, is "payable ... by the producer or manufacturer at the time when the goods are delivered to the purchaser or at the time when the property in the goods passes, whichever is the earlier." The evidence established, to the satisfaction of the Tribunal, that invoice No. 16268, pertaining to shipments to Park Lane, concerned goods delivered before July 1, 1985; consequently, the goods in that invoice are not subject to sales tax. As delivery occurred prior to the date of introduction of the tax, it is unnecessary to establish the date when property passed.

For the other transactions at issue, delivery was made after June 30, 1985. It is, therefore, necessary to determine the date when property passed. All of the transactions are governed by the Ontario *Sale of Goods Act*.⁶ That Act provides that property in goods passes when the parties to a contract intend it to pass.

On the question of intention, the Tribunal gave considerable weight to the provision on the appellant's invoices that provides that property passes only after payment is made. Mr. Wiley testified that this provision did not govern the appellant's dealings with its customers. However, the Tribunal has difficulty with relying solely on the uncorroborated testimony of the witness regarding what was in the minds of the appellant's customers. In the absence of corroborating testimony, the Tribunal is of the view that it should consider at face value the plain and unequivocal wording of the invoice. Considering the words on that basis, the Tribunal concludes that the express terms of the contract reflect the intention of the parties and that property in the insulation passed when payment was made (i.e. after July 1, 1985). Consequently, all transactions where the delivery of the goods in issue occurred after June 30, 1985, are subject to sales tax.

For the foregoing reasons, the appeal is allowed in part.

Kathleen E. Macmillan
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6. R.S.O. 1980, c. 462.