



Volume 15 Number 3

July 2008

State Tax Return

Georgia Supreme Court Denies Refunds of Sales Tax for Repair Parts

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By a slim majority, the Georgia Supreme Court recently overruled a Georgia Court of Appeals decision and held in *Georgia Department of Revenue v. Owens Corning*¹ that the version of O.C.G.A. § 48-8-3 (the “Exemption Statute”) in effect from July 1, 1997 through December 31, 2000 did not provide an exemption from sales and use tax for machinery repair parts. Owens Corning, which filed a claim seeking a refund of taxes paid on repair parts from 1997-1999, asserted that the exemption provided for “[m]achinery, *including components thereof*” encompassed repair parts. The Supreme Court disagreed and denied Owens Corning’s claim relying in large part upon the perceived legislative history of the Exemption Statute. A well reasoned dissent filed by three of the seven justices contended that the majority had fundamentally erred in its analysis by failing to correctly apply the rules of statutory construction.

Evolution of the Exemption for Machinery Repair Parts

Beginning in 1951, when the Georgia General Assembly enacted the Retailers’ and Consumers’ Sales and Use Tax Act, and for more than 40 years thereafter, machinery repair parts were subject to sales and use tax. Then in 1994, the Georgia Legislature amended the Exemption Statute to provide an exemption from sales and use tax for “[m]achinery which is used directly in the manufacture of tangible personal property when the machinery is bought to replace or upgrade machinery in a manufacturing plant presently existing in this state”² (the “1994 Amendment”).

In 1997, the Georgia General Assembly again amended the Exemption Statute to exempt “[m]achinery, *including components thereof*, which is used directly in the manufacture of tangible personal property when the machinery is bought to replace or upgrade machinery in a manufacturing plant presently existing in this state”³ (the “1997 Amendment”). Neither the Legislature nor the Department of Revenue defined the meaning of “components.”

¹ *Georgia Department of Revenue v. Owens Corning*, No. S07G1297, 2008 WL 1773612 (Ga. Apr. 21, 2008) (*reconsideration denied* May 19, 2008).

² Ga. L. 1994, pp. 929, 930 § 5.

³ Ga. L. 1997, pp. 1412, 1413 § 1 (emphasis added).

Finally, during the 2000 legislative session, the General Assembly enacted a phased-in exemption for the “sale or use of repair or replacement parts . . . for machinery used directly in the manufacture of tangible personal property in a manufacturing plant presently existing in this state”⁴ (the “2000 Amendment”). The exemption provided by the 2000 Amendment was effective for all calendar years beginning on or after January 1, 2001.⁵ The exemption for “machinery” and the “components thereof” was not eliminated by the 2000 Amendment, but the Exemption Statute was modified to provide an exemption for:

Machinery which is used directly in the manufacture of tangible personal property when the machinery is bought to replace or upgrade machinery in a manufacturing plant presently existing in this state and *machinery components which are purchased to upgrade machinery* used directly in the manufacture of tangible personal property in a manufacturing plant.⁶

Although it was unclear whether the term “machinery,” as used in the 1994 Amendment, exempted machinery repair parts, the Georgia Court of Appeals ruled in *Inland Paperboard & Packaging, Inc. v. Georgia Department of Revenue*⁷ that the term “machinery” means a machine in its entirety and does not include or refer to the machine’s constituent parts.⁸ The *Inland* court reasoned that “[s]ince the 2000 version of the Exemption Statute *for the first time* expressly exempted repair and replacement parts from taxation, it follows that such parts were *not* exempt under the 1994 version.”⁹ The *Inland* court failed to consider, however, the effect and intent of the 1997 Amendment. If, as the *Inland* court held, the 1994 Amendment did not exempt machinery repair parts and the 2000 Amendment provided such an exemption “for the first time,” what could “machinery, *including components thereof*” mean? The Court of Appeals took up this question in *Owens Corning v. Georgia Department of Revenue*.¹⁰

In *Owens Corning*, the Court of Appeals acknowledged that *Inland* had “only compared the 1994 version of the statute with prior versions of the statute and with the 2000 version; it did not consider or address the effect of the 1997 Amendment.”¹¹ As a result, *Inland* was not controlling.¹² The Court of Appeals then “read the 1997 version of the statute to continue to provide a sales tax exemption for the designated machinery bought to replace or upgrade existing machinery *and to expand that exemption to also*

⁴ Ga. L. 2000, pp. 615, 616 § 2.

⁵ *Id.*

⁶ Ga. L. 2000, pp. 615, 615 § 1 (emphasis added).

⁷ 274 Ga. App. 101 (2005).

⁸ *Id.* at 102.

⁹ *Id.* at 104 (emphasis added).

¹⁰ 285 Ga. App. 158 (2007).

¹¹ *Id.* at 159.

¹² *Id.*

include components of designated machinery bought to replace or upgrade existing machinery.”¹³ As a result, repair and replacement parts were exempt from sales tax under the Court of Appeals’ interpretation of the 1997 Amendment. The Department of Revenue applied for further appeal, and the Georgia Supreme Court granted certiorari.

The Supreme Court Decision

Rather than basing its decision on the language of the 1997 Amendment, as might have been expected, the Georgia Supreme Court grounded its decision in *Owens Corning* on what it perceived to be the legislative history of the Exemption Statute.¹⁴ Citing the 1951 Retailers’ and Consumers’ Sales and Use Tax Act, the court noted “[a]t the outset . . . we begin [in 1951] with a clear and unambiguous legislative intent that machinery repairs parts are not exempt from sales tax.”¹⁵ The Court then noted that the 1994 Amendment contained “no reference to machinery repair parts” and thus “no exemption existed under this language.”¹⁶ Continuing to describe the evolution of the Exemption Statute, the Court noted that the 1997 Amendment provided a sales tax exemption for “[m]achinery, including components thereof.” Yet, without attempting to define the term “components,” the Court concluded that “[n]othing in this language [of the 1997 Amendment] creates an explicit exemption from sales tax for machinery repair parts. At best, this language may create some ambiguity that ‘replacement components’ could possibly include repair parts.”¹⁷

Turning again to the history of the Exemption Statute, the Court concluded that “in light of the Legislature’s explicit past declarations that machinery repair parts should be subject to tax, it stands to reason that, if the Legislature wished to reverse this historical trend in the 1997 Amendment, it would have done so explicitly.”¹⁸ Thus, the Court expected the Legislature to include the explicit phraseology “repair parts” in the 1997 Amendment rather than the term “components” to provide an exemption for machine parts. Taxpayers can be forgiven for wondering why the term “components” did not nonetheless provide an exemption for repair or replacement parts within its ordinary meaning.

The dissent rejected the majority’s overly restrictive approach to interpreting the 1997 Amendment: “The initial flaw in the majority’s analysis is that, rather than properly focusing on the controlling ‘literal language’ of [the Exemption Statute], it relies instead on pre-1997 law to demonstrate that an ambiguity exists as [to] the meaning of ‘components.’”¹⁹ Citing the Georgia Supreme Court’s precedent, the dissent noted that “the ‘golden rule’ of statutory construction . . . requires us to follow the literal language of the statute unless it produces contradiction, absurdity, or such an inconvenience as to

¹³ *Id.* at 160 (emphasis added).

¹⁴ *Georgia Dep’t of Revenue v. Owens Corning*, No. S07G1297, 2008 WL 1773612 (Ga. Apr. 21, 2008).

¹⁵ *Id.* at *1.

¹⁶ *Id.*

¹⁷ *Id.* at *2.

¹⁸ *Id.*

¹⁹ *Id.* at *4.

insure that the legislature meant something else.”²⁰ The dissent noted that the term “component” is not a term of art. Rather, a “component” simply refers to a “constituent element, as of a system” and a “part of a mechanical or electrical complex.”²¹ In other words, the definition of a “component” easily encompasses the individual parts of a machine. The dissent noted that the majority “begins its analysis with the unwarranted assumption that the term ‘components’ . . . is ambiguous, and then attempts to justify that assumption.”²²

The dissent also attacked the majority’s reliance on the 2000 Amendment. The majority concluded:

The Legislature’s intent that the exemption for machinery repair parts not take effect until 2000 is made evident from the stated purpose for the 2000 statutory revision, namely “to amend Code Section 48-8-3 . . . , relating to exemption from sales and use taxes, so as *to clarify* that the exemption regarding certain components of machinery used directly in the manufacture of tangible personal property extends only to machinery components purchased to upgrade such machinery.”. . . The Legislature then goes on to create a prospective phased-in exemption for machinery repair parts. This language shows that the Legislature wished to eradicate any ambiguity caused by the 1997 statute and make it clear that the 1997 statute did not extend the sales tax exemption to machinery repair parts.²³

The dissent notes, however, that what is being “clarified” is subject to dispute:

[T]he General Assembly recognized that the 1997 exemption granted to “components” was unambiguously broad enough to include repair parts and, in 2000, it changed that by amending the statute to provide otherwise. Thus, the clear legislative intent of the 2000 statute was “to clarify” that the former broad exemption for “components” granted under the 1997 version would no longer apply after the effective date of the amendment to OCGA § 48-8-3(34)(A). . . . If the majority were correct, then the General Assembly could always effect a retroactive substantive change in the law simply by enacting a subsequent amendment so as “to clarify” that a statute had an entirely different meaning than

²⁰ *Id.* (quoting *TELECOM*USA v. Collins*, 260 Ga. 362, 363 (1990)) (internal quotation marks omitted).

²¹ *Id.* (quoting American Heritage Dictionary 302 (2d College ed.)).

²² *Id.*

²³ *Id.* at *2.

that which was conveyed by the unambiguous language of its previous provisions.²⁴

Conclusion

The Georgia Supreme Court's majority opinion adopted a niggardly approach to the application of the exemption for components granted by the General Assembly in the 1997 Amendment. Had the Court followed the rules of statutory construction, the 1997 Amendment could have easily exempted repair parts. The 1997 Amendment, however, will not continue to plague Georgia taxpayers since repair parts became fully exempt from sales and use tax on January 1, 2005. While the majority decision may be wrong (in the authors' humble opinions), its impact will be limited.



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²⁴ *Id.* at *7.