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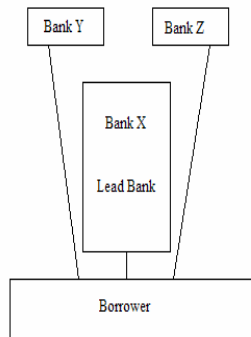
Does an agent / lead bank stand in fiduciary relation when dealing with syndicate members?

by Roy Santanu.¹

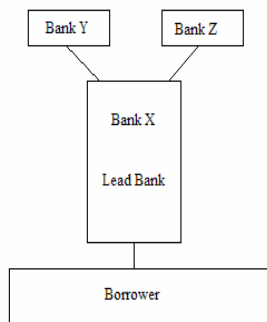
Syndicate: Syndicate is the process by which a company or project can be financed. Normally the value of the project or the risk involved is so high that no one bank wants to do it alone.

Bank Syndicate: A bank syndicate comprises a number of banks associated to carry out some business. Bank Syndicate may be of two types:

True Syndicate: Here each bank enters into a direct relationship with the borrower. There may be more than one lead bank.



Participation Syndicate: In this type of syndicate the lead bank enters into a relationship with the borrower. Then the lead bank sells participations in the loan or security to other banks. Here, the other banks are not in a direct relationship with the borrower.



In the case of First National Bank v. Cont'l Ill. National Bank and Trust Co.² we find a contractual dispute between two banks who participated in a joint lending arrangement of the kind known as a participation agreement.

In such type of participation, one bank (the 'lead bank') first makes the loan agreement with the borrower and then the lead bank makes separate agreements with other banks, to which the lead bank sells shares in the loan, evidenced by participation certificates. The result is that only the lead bank has a direct contractual relationship with the borrower.

There are four legal characterization of a syndicate:

1. It is a partnership between the banks
2. There is a joint venture in jurisdictions' laws
3. There is a contractual relationship governed by the terms agreed between the banks.
4. It gives rise to a fiduciary relationship between the lead bank and the members of the syndicate.

In UBAF Ltd v. European American Banking Corporation (EAB)³, we find that fiduciary duty in a syndicated loan of a lead bank is a continuing duty and does not come under section 32(1) (b) of the Limitation Act 1980, U.K. The facts of the above case in brief are as follows; UBAF Ltd., an English Bank, was invited by an American bank to participate in two loans of two companies which were part of a shipping group.

The Assistant Secretary of the American Bank sent information about the loan to the English Bank. The information was a study of the shipping companies. The English Bank claimed that based on that information the loans were attractive to finance. As a result, in due course the loan was made and there was a default in payment and due to this default the English Bank charged the American Bank with deceit, misrepresentation and negligence in making the representations. The question put forward in this case was that whether signature of a bank's Assistant Secretary constitute signature of a bank or not.

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² 933 F.2d 466.

³ [1984] 1 QB 713

Section 6 of the Frauds Amendment Act 1828, UK, states that: “No action shall be brought whereby to charge any person upon or by reason of any representation or assurance made or given concerning or relating to the character, conduct credit, ability, trade or dealings of any other person to the intent or purpose, that such other person may obtain credit, money or goods, unless such representation or assurance be made in writing, signed by the party to be charged therewith.”

It was held by Ackner and Oliver L.JJ. that the signature of the American Bank's Assistant Secretary did constitute the signature of the bank as because he was an authorised agent of the Bank who was acting within the scope of his authority. The second question which was raised was that, did the American Bank have a fiduciary duty to the English Bank or was the duty barred by Limitation.

It was held that “for the purpose of limitation the fiduciary duty on a lead bank was a continuing duty and it would be a question of fact for determination at trial whether EAB [American Bank] had in fact come to know at any stage that the security for the loan was inadequate.” Some commentators say that the lead bank is initially the agent of the borrower, but when the syndicate is put together, it becomes agent of the syndicate members and thus owes them fiduciary duties.

English Common law requires circumstances in which the lead bank will owe a fiduciary duty to the syndicate. However, in *Banque Arabe Et Inertnationale D'Investissement v. Maryland National Bank*⁴, we find that, in the case of arm's length transactions between large financial institutions, no fiduciary duty exists unless one was created in the agreement.

In the US case of *First Citizens Federal Savings and Loan Association v. Worthen Bank and Trust Company*⁵, First Citizens Federal Savings and Loan Association (**FC**), Worthen Bank and Trust Company (**WC**) and 20 other savings and loan institutions entered into a loan participation agreement in connection with a real estate development. The borrower ultimately defaulted and the participants incurred losses. FC filed action, alleging breach of contract, negligence, negligent misrepresentation and constructive fraud through breach of fiduciary duty and securities fraud by WC in its role as principal; the remedy sought was rescission.

Now-a-days fiduciary duties are moulded by their contractual settings. Therefore a syndicate

loan may make it clear that the lead/agent bank need not disclose the sums received for its own account. Furthermore, a clause may protect the lead bank if in its judgement it decides not to disclose to the syndicate certain of the confidential information it has obtained from the borrower. It may be said that nothing by itself puts the lead bank in fiduciary relationship with the syndicate.

End.

FAQ's on Value Added Tax – Some Frequently Asked Questions

by Chowdhury Amarnath.⁶

Value Added Tax (**VAT**) has made its way in most of the States in India with effect from 1st April, 2005, amidst stiff resistance from many segments of trading community. VAT is prevalent in most of the countries world over and offers many advantages.

1 What is Value Added Tax? What are the characteristics?

- 1.1 VAT is a multipoint tax on value added at each stage with set off input tax credit paid on purchase of new material.
- 1.2 VAT helps collection of tax in each stage of the production and distribution process.
- 1.3 VAT is on the consumer and not for the dealer.
- 1.4 VAT is a destination based levy.
- 1.5 VAT is progressive taxation system.
- 1.6 VAT has got no cascading effect due to credit mechanism.

2 Advantages of VAT?

- 2.1 Eliminates double taxation (cascading effect).
- 2.2 Increases Tax base.
- 2.3 Ensures collection of tax on full value creation.
- 2.4 Removes multiple tax bases like surcharge, turnover tax, special additional tax etc.
- 2.5 Promotes self policy mechanism (voluntary compliance).

⁶ **Chowdhury Amarnath** (LL.B. ACS) is an Associate of Saha & Ray. He may be reached at amaranth.chowdhury@saharay.com

- 2.6 Ensure efficient tax collection.
- 2.7 Results in revenue buoyancy.
- 2.8 Reduces tax evasion.
- 2.9 Provides simple, stable and transparent tax system.
- 2.10 Ensures that there is no tax war between the States.
- 2.11 Tax payer friendly approach.

3 What is the difference between VAT and the Existing Sales Tax (**ST**)?

- 3.1 In ST, first point and last point were taxable. VAT is multipoint taxation.
- 3.2 In ST, the Rate of Tax is multiple. However, in VAT it is much more rationalised, i.e. 1% only for Gold and Silver ornaments, 4% for 270 items including declared goods, drugs, medicines, industrial product, all agricultural and industrial inputs and Capital goods, and 12.5 % for all other goods. Aviation turbine fuel, petroleum products, liquor lottery tickets and other spirit will be out of VAT 'regime'.
- 3.3 In ST, dealing was possible only in items that were mentioned in the Registration Certificate (**RC**) but in VAT any item can be dealt with. It is not required to mention Commodities on the RC in VAT.
- 3.4 In ST, local forms are used in large quantities. It led to unnecessary hardship to dealers and frequent visit to Sales Tax Department (**STD**) but in VAT no statutory local form, except Road Permit and CST form is required and this reduces visit to the STD.
- 3.5 In ST, assessment is mandatory, but in VAT it is self assessed and weightage is given to audit work in place of assessments.
- 3.6 In ST, no input Tax Credit is allowed but in VAT Tax Credit is allowed only if the purchase is from a registered dealer. If the purchase is local and the goods are used for sale and resale, inter state sale/export, used in the manufacturing process and packing, there is no input Credit Tax Credit if the raw material is used for the manufacture of

⁴ 819 F. Supp. 1282,

⁵ 919 F.2d 510

<p>exempted goods, as in case of inter state purchase and if the purchase is made from unregistered dealer without providing tax invoice.</p>	<p>6 Can one avail Tax credit on stock transfer under VAT scheme?</p>	<p>10.3 VAT on Works Contract pertaining to transfer of property in goods is liable to tax on the Contractual Transfer Price (CTP). CTP is the amount received or receivable for transfer of property in goods in execution of Works Contract. The following is reduced from the value of contract to arrive at CTP:</p>
<p>3.7 In ST, normal invoice is used but in VAT two kinds of invoice are used: (i) Tax Invoice - on the basis of which the purchasing dealer can claim input tax credit and; (ii) Retail Invoice. No credit of tax can be claimed on the strength of a Retail Invoice. Retail Invoice are generally issued by registered dealer to consumer, and by unregistered dealer to registered dealer/ unregistered dealer and in inter-state sale.</p>	<p>6.1 In case of stock transfer, input tax would be eligible for tax credit. Tax paid on inputs procured from other states through stock transfer or inter state will not be eligible for credit.</p>	<p>(a) value of exempted goods (b) value of sub-contract(subject to conditions) (c) labour charges (d) cost of certain consumables (e) hire charges of certain machinery (f) administrative charges proportionate to labour charges (g) cost of designing, fees, etc.</p>
<p>3.8 In ST, registration is required for every dealer who deals in taxable goods and whose turnover exceeds the threshold limit but in VAT there are two types of registration - one is compulsory registration and the second is voluntary registration. Compulsory registration is required for dealers having turnover above a threshold limit of Rs 5 lacs. Voluntary registration is required for dealers having turnover below the threshold limit. The threshold limit will vary from state to state. The existing dealers will automatically get registered under the VAT Act. New eleven digits TIN (Tax Identification Number) will be allotted to all the dealers. A Compounding scheme can also be availed by the dealers having turnover between Rs 5 lacs to 50 lacs, by paying 1% on total turnover without availing input tax credit.</p>	<p>7 Is Central Sales Tax Act 1956 (CST) still in vogue?</p> <p>7.1 CST would be abolished in phases after 2005-06 i.e. C Form, D Form, E1 and E2 Form, F Form is still there.</p> <p>7.2 There will be no input credit in case of inter-state purchase of goods.</p> <p>8 What happens to the opening stock of goods lying as on 31st March 2005?</p> <p>8.1 All tax paid on purchase from 1st April 2004 to 31st March 2005 and still in stock will be eligible to receive input tax credit subject to submission of requisite details.</p> <p>8.2 Proof of payment of tax will be needed.</p> <p>8.3 100% input credit where tax paid is clearly mentioned in the invoice; otherwise 75% of tax paid is considered inclusive.</p>	<p>VAT on Works Contract is levied @ 4% on the value of CTP.</p> <p>10.4 The government has simplified the process of dealers and work contractors and henceforth assessment would be done on the basis of self assessment instead of scrutiny. Use of various kinds of form for purchases on lower rate of taxes has been removed, thereby further simplifying the process. Besides this, the government had introduced two simple schemes:</p>
<p>4 What is to be done with Tax credit, which exceeds the tax collection in a month?</p> <p>4.1 If the Tax Credit exceeds the tax collection in a month on sales within the state or in inter- state sale, the excess credit will be carried over to the next month. Tax credit will be carried upto the end of the next financial year. Excess, unadjusted tax credit if any, will be eligible for refund. Tax paid on capital goods will be eligible for tax credit.</p>	<p>9 Is audit compulsory in VAT?</p> <p>9.1 The Act envisages correctness of self-assessment through a system of audit.</p> <p>9.2 It also envisages the selection of audit by a scientific criterion.</p> <p>9.3 VAT audit is compulsory if turnover exceeds Rs 40 lakhs.</p> <p>9.4 Audit shall be at business premises.</p> <p>9.5 In case of evasion, there will be assessment for all the previous periods up to last 5 (five) years.</p> <p>9.6 There shall be an independent audit wing.</p>	<p>a) Scheme for payment of tax at compounded rate of 2%. The contractor can, subject to condition, once a year opt for the scheme and pay tax @ of 2% of the total contract value. He shall not be entitled to claim any input credit, however he can set off this with the VAT deducted at source @ 2% by the promoter.</p>
<p>5 Is VAT levied on exports?</p> <p>5.1 For all exports made out of the country, tax paid within the state will be refunded in full within three months from the date on which the new levy is paid. Units located in SEZs and EOUs would be exempted from VAT, which are all set to be ushered in. In case exemption is not possible, refund would be provided in three months.</p>	<p>10 How is VAT on Works Contract calculated?</p> <p>10.1 Sales Tax on Works Contract has been replaced by VAT on Works Contract with effect from 1st April 2005.</p> <p>10.2 VAT on works contract is applicable only when there is transfer of property in goods in the execution of works contract by a contractor.</p>	<p>b) Where the accounts are not maintained in a manner where the CTP can be ascertained properly, the government has specified certain fixed percentage for different kinds of work contract which would be deducted from the contract value to the CTP.</p>

11 Is VAT applicable on works contract in joint development of property wherein the land owner and the developer come together to develop a property?

11.1 VAT on the Works Contract becomes applicable when a promoter appoints a contractor for a project and it is here that the connection between real estate and VAT comes into picture.

Conclusion:

- 1 Inter-state purchases could prove to be costlier than local procurements as no input credit is available on inter state purchase.
- 2 In case of stock transfer, input tax credit will be adjusted against the VAT liability, i.e. stock transfer will not be encouraged.
- 3 Input tax credit on capital goods purchase is available.
- 4 There is incentive to buy only from registered dealers. For those who have been complying with tax laws, VAT would be a boon that reduces the cost of product to the customer and boosts competitiveness.
- 5 In self assessment, great care should be exercised in filing the return with the Department.
- 6 The Industry and trade gain from transparency and the need to interact with the tax personnel is reduced.
- 7 Penal provisions on VAT will not be more stringent than the existing sales tax.
- 8 Implementation of VAT system does not mean that a dealer has to adopt a new system of accounts but he has to simply keep records for claiming adjustments or setting off previous tax paid. Under VAT, dealers will have to make two more entries - input tax (tax paid on purchases) and output tax (tax charged on sales) as the same is mandatory.

End.

NOTIFICATIONS:

Ministry: Ministry of Finance

Department/Board: Service Tax

Notification No: 15/2005

Date: 07.06.2005

Enforcement of Clauses (a) and (b) of Section 88 of the Finance Act, 2005

In exercise of the powers conferred by clause (a) and clause (b) of section 88 of the Finance Act, 2005 (18 of 2005), the Central Government hereby appoints the 16th day of June, 2005 as the date on which the provisions of the said clauses of the said Act shall come into force.

End.

Ministry: Ministry of Finance

Department/Board: Service Tax

Notification No: 18/2005

Date: 07.06.2005

Exemption in relation to Construction of Complex

1. In exercise of the powers conferred by sub-section (1) of section 93 of the Finance Act, 1994 (32 of 1994) (hereinafter referred to as the Finance Act), the Central Government, on being satisfied that it is necessary in the public interest so to do, hereby exempts the taxable service provided to any person by any other person, in relation to construction of complex, referred to in sub-clause (zzzh) of clause (105) of section 65 of the Finance Act, from so much of the service tax leviable thereon under section 66 of the said Finance Act, as is in excess of the service tax calculated on a value which is equivalent to thirty-three per cent of the gross amount charged from any person by such service provider for providing the said taxable service:

Provided that this exemption shall not apply in such cases where –

- (i) the credit of duty paid on inputs or capital goods used for providing such taxable service has been taken under the provisions of the CENVAT Credit Rules, 2004; or
- (ii) the service provider has availed the benefit under the notification of the Government of India, in the Ministry of Finance, (Department of Revenue) No. 12/2003-Service Tax, dated the 20th June, 2003

[G.S.R. 503 (E), dated the 20th June, 2003]; or

- (iii) the taxable services provided are only completion and finishing services in relation to residential complex, referred to in sub-clause (b) of clause (30a) of section 65 of the Finance Act.

Explanation.

For the purposes of this notification, the “gross amount charged” shall include the value of goods and materials supplied or provided or used for providing the said taxable service by the said service provider.

2. This notification shall come into force on the 16th day of June, 2005.

End.

Legal Quotations.

The law and medicine should be very serious professions to undertake, should they not? People's lives and fortunes depend on them.

George Eliot.

It ain't no sin to crack a few laws now and then, just so long as you don't break any.

Mae West.

There's no better way of exercising the imagination than the study of law. No poet ever interpreted nature as freely as a lawyer interprets truth.

Jean Giraudoux.

We wouldn't have been nicked if you'd kept your mouth shut. Making us look ridiculous by telling the truth. Why can't you lie like a normal man?

Joe Orton – Loot.

The Common Law of England has very laboriously been built about a mythical figure of 'the reasonable man'. An Act of God has been defined as 'something which no reasonable man could have expected'.

A.P. Herbert.

He is always breaking the law. He broke the law when he was born: his parents were not married.

George Bernard Shaw – Major Barbara.