

Chapter 14

Foreign Exchange Management Act, 1999

Short forms used:

| | | | |
|------|---------------------------------|-------|-------------------------------|
| AD | Authorized Dealer | Forex | Foreign Exchange |
| AP | Authorized Person | Forse | Foreign Securities |
| BOA | Branch, Offices and Agencies | IC | Indian Currency |
| CAT | Capital Account Transaction | LRS | Liberalised Remittance Scheme |
| CUAT | Current Account Transaction | PRI | Person Resident In India |
| FC | Foreign Currency | PROI | Person Resident Outside India |
| FEMA | Foreign Exchange Mgt. Act, 1999 | TC | Travellers' cheque |

Purpose of the Act:

An Act to **consolidate** and amend the law relating to foreign exchange with the **objective** of:

- **facilitating** external trade and payments and
- for **promoting** the orderly **development** and **maintenance** of forex market in India

With liberalization of Indian economy in 1991, the flow of Forex into India increased thus increasing the Foreign Exchange Reserve (FER) substantially. This act enables mgt. of FER for the country.

Enforcement of the Act - Directorate of Enforcement (ED)

Forex Regulation Act 1947, 1973 vs FEMA 1999:

| | FERA | FEMA |
|------------------------|--|--|
| Objective of Act | Conserve Forex | Promote and develop the forex |
| PRI | Based on citizenship | Based on stay in India |
| Strictness | Forex transaction is prohibited unless permitted | Forex transaction is permitted unless restricted |
| Mens-rea (guilty mind) | Presumption of existence of mens-rea | Mens-rea not presumed. Responsibility of prosecution to prove |
| Compounding of offence | Not allowed | All offences are compoundable |

Broad Division of Act:

| | | | | | | |
|--------------------------|------------------------------------|----------------------------------|--|--|---|----------------------|
| Preliminary [Sec 1-2] | Reg and Mgt. of Forex [Sec 3-9] | Authorised Person [Sec 10-12] | Contravention and Penalty [Sec 13-15] | Adjudication and Appeal [Sec 16-35] | Directorate of Enforcement [Sec 36-38] | Misc. [Sec 39-49] |
|--------------------------|------------------------------------|----------------------------------|--|--|---|----------------------|

Sec 1: Applicability

This Act extends to **whole of India**. Also applies to all BOA **outside India** owned or controlled by **PRI**



Sec 2: Definition

- Authorised Person [Sec 2(c)] means an:

Authorised
Dealer (AD)

Money
Changer

Off-shore
banking unit

Other person auth. u/s 10
to deal in Forex or Forse

- Foreign Currency [Sec 2(m)] means any currency other than Indian Currency

- Foreign Exchange [Sec 2(n)] means Foreign Currency and includes:

Deposits, credits and
bal. payable in any FC

Draft, TC, LoC, BoE drawn
in IC but payable in FC

Drafts, TC, LoC, BoE drawn by Banks or
Person outside India but payable in IC

- Foreign Security [Sec 2(o)] means:

- o Any **security** in the form of - Stock, shares, bond, debentures or other inst.
- o **Denominated** in FC,
- o And includes - Sec. denominated in FC but redemption or returns (int./div) payable in IC

- Capital Account Transaction [Sec 2(e)]: means a transaction which **alters**:

- a. Asset or Liabilities (incl. contingent liability) o/s India of PRI
- b. Asset/Liability in India of PROI

- Current Account Transaction [Sec 2(j)] means transaction other than CAT

Without prejudice to the generality of the definition, CUAT includes:

Payments w.r.t., foreign
trade, current business,
services, & **short-term**
banking & credit facility
in **OCOB**

Payments w.r.t.,
interest on
loans & as net
income from
investments

Remittances for
living expenses of
parents, spouse and
children residing
abroad

Expense w.r.t.
foreign **travel**,
education and
medicare of parents,
spouse and children

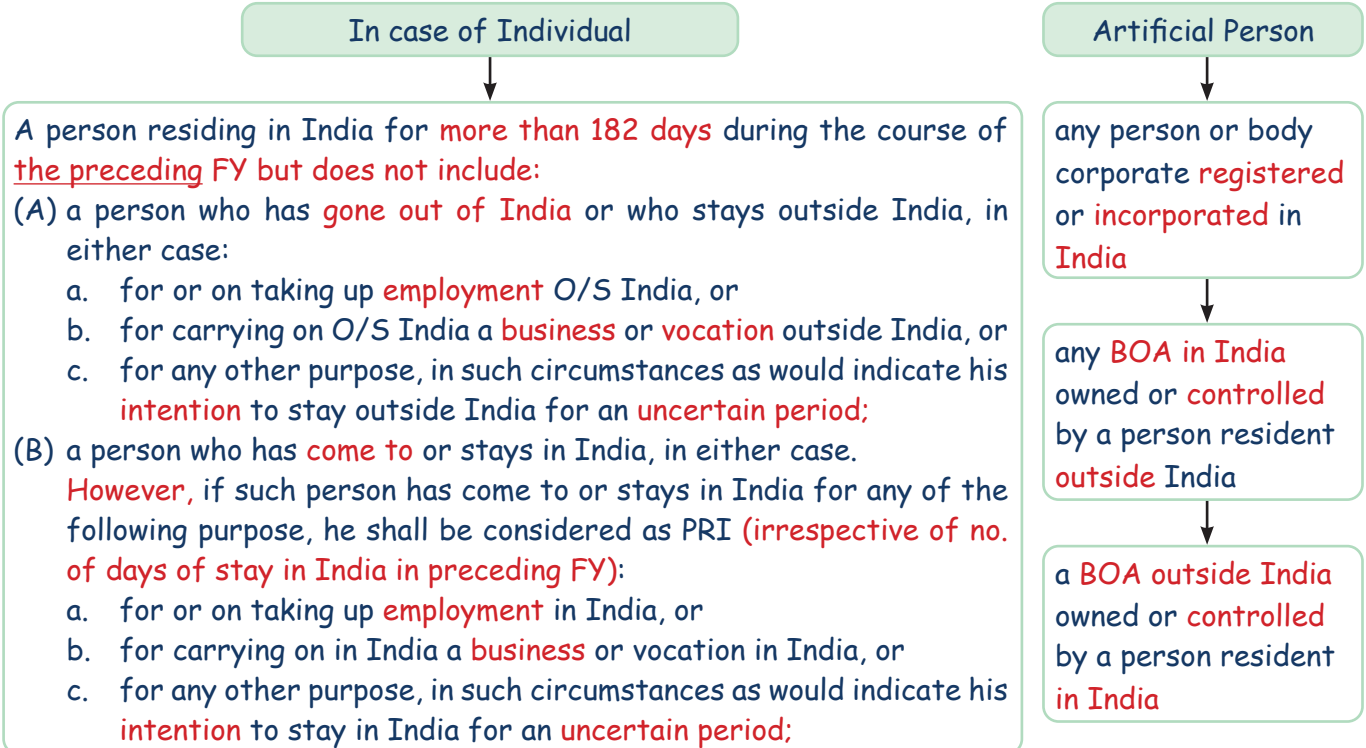


Section 2(u) - "Person" includes:

- i. an individual,
- ii. a HUF,
- iii. a company,
- iv. a firm
- v. an association of persons or body of indv., (incorporated or not)
- vi. every artificial juridical person, and
- vii. **any agency, office or branch owned or controlled by such person;**



Section 2(v) – “Person Resident in India” means:



Section 2(w) – “Person Resident outside India” means a person who is not Resident in India

Concept Clarity Check:

- Citizenship** is not relevant for determining PRI or PROI
- If in FY 2019-20, a person resides in India for 200 days. On 1st June 2020, the person leaves India for employment o/s India. Determine whether PRI or PROI? - **For the period 1st April 2020 to 1st June 2020, such person shall be PRI and from 2nd June 2020 onwards, he will be a PROI (irrespective of the fact that he resides for more than 182 days in preceding FY)**
- Mr. S comes to India on 1st June 2019 for visiting his parents. However, his parents fall sick and he is certain that he will not be able to return for an year. He ends up staying with them till 31st July 2020. Is he a PRI in FY 20-21? - **No, in FY 20-21, Mr. S will be considered as PROI. Even though he resided in India for more than 182 days in FY 19-20, he has not come for any of the 3 purpose (employment, business or uncertain period) and hence he is not a PRI in FY 20-21**
- Residential status is **not for a year**. It's on a particular date. (Unlike Income Tax Act, 1961)
- Is it mandatory for a person to reside in India for more than 182 days in the previous FY to be considered as PRI? - **Umm, No. If he resides for <=182 days in preceding FY, but comes to India in the current year for the 3 purpose, he will become PRI in current year.**
- Where a student is leaving India for **higher studies**, RBI has clarified that they shall be **treated as PROI** majorly because of their intention to stay outside India for an uncertain period and the fact that they start working there to take care of their expenses



Sec 3: Dealing in Foreign Exchange, etc.

No person (PRI & PROI) shall:

Deal in or transfer
Forex or Forse to any
person other than AP

make any
payment to/for
credit of PROI

Receive any payment
from PROI otherwise
through an AP*

Enter into Financial Transaction
in India as consideration for
acq. of asset o/s India

*Where any such payment is received without corresponding inward remittance, it shall be deemed to be received through person other than AP

However, the above restricted transactions may be carried on:

- If otherwise provided in this Act, Rules or Regulation, or
- With permission of RBI (general or special)

Note -

- For this section - Financial transaction means:

payment to/credit
of any person or

receiving payment for or
on behalf of any person or

to draw/issue/
negotiate any BoE or

trf. security or
acknowledge debt

- Purpose of this section is to regulate inflow and outflow of Forex in regulated manner and through APs only.



Sec 4: Holding of Forex

Except as provided in this Act, no PRI shall Acquire, Hold, Own, Possess or Transfer [HA! TOP] any Forex, Forse or Immovable Property situated o/s India.



Sec 5: Current Account Transactions:

Any person may sell or draw Forex to or from an authorised person if such sale or drawal is a CUAT.

CG may, in consultation with RBI, impose reasonable restrictions on CUAT.

Note: RBI cannot, on its own, impose any restriction on current account transaction. Restrictions can be imposed only by CG (in consultation with RBI)

Examples of CUAT:

- Import in India of machinery for installation in factory from a UK vendor by payment in cash
- Import in India of machinery for installation in factory from a UK vendor on credit for 3 months (this is CUAT because short term banking and credit facilities covered as CUAT)
- Gift (say \$1,000) by a PRI to PROI (note: Gift is given in FC)
- Gift (say Rs. 1,000) by a PRI to PROI in India - This will be a CAT and not CUAT as this results in alteration of asset of the PROI in India. Although it is a CAT, such gifting is permitted as per Rules.

General Rule:

CUAT is freely permitted unless specifically restricted.



Schedules of FEM(CUAT) Rules, 2000

**Schedule I** - Drawal of forex by any person for following purpose is prohibited:

1. Remittance out of lottery winnings,
2. Remittance of income from Racing/riding etc. or any other hobby,
3. Remittance for purchase of lottery tickets, banned magazines, football pools, sweepstakes etc.,
4. Payment of commission on exports made towards equity investment in JV / WOS abroad of Indian cos.,
5. Remittance of dividend by any co. to which the requirement of dividend balancing is applicable,
6. Payment of commission on exports under Rupee State Credit Route, except commission upto 10% of invoice value of exports of tea and tobacco.
7. Payment related to "Call Back Services" of telephones,
8. Remittance of interest income on funds held in Non-Resident Special Rupee Account Scheme

[i.e., if any of the above remittance/payments is to be done by a PRI to a PROI, the PRI cannot go to AP and draw \$s because these are prohibited]

**Schedule II** Schedule II - Transactions which require prior approval of GoI for drawal of forex

| Purpose of Remittance | Ministry / Dept. of GoI who approval is required |
|--|---|
| Cultural Tours | Ministry of Human Resources Development, Dept. of Education and Culture (Now known as Ministry of Education) |
| Advt. in foreign print media by a SG & its PSUs > \$ 10K Except where such advt. is for the purposes of promotn of tourism, foreign investments and international bidding <u>Note: PSUs of CG not covered!</u> | MoFinance, Dept. of Economic Affairs |
| Remittance of freight of vessel chartered by a PSU | MoSurface Transport, Chartering Wing |
| Payment of import (through ocean transport) by a Govt. Department or a PSU on C.I.F. basis (i.e., other than F.O.B and F.A.S. basis) | MoSurface Transport, Chartering Wing |
| Multi-modal transport Operators making remittance to their agents abroad | Registration Certificate from Director General of Shipping |
| Remittance of hiring charges of transponders: | |
| a. TV Channels | Ministry of Info and Broadcasting |
| b. Internet service providers | Min. of Communication & Info. Tech |

| | |
|---|---|
| Remittance of container detention charges > the rate prescribed by Director General of Shipping | Ministry of Surface transport (Director General of Shipping) |
| Remittance of prize money / sponsorship of sports activity abroad by a person other than International/ National/State Level sports bodies, if the amt. involved > US\$ 100,000 | Ministry of HR Development, Dept of Youth Affairs & Sports (Now - Mo Youth Affairs and Sports) |
| Remittance for membership of P & I Club (protection and indemnity insurance) | Ministry of Finance (Insurance Division) |



Schedule III

Transactions which in excess of limits require prior approval of RBI for drawal of forex: [Liberalised Remittance Scheme]

1. Individuals - Avail forex facility for the following purpose within limit of **USD 2,50,000 only**. Additional remittance **beyond limit** shall **require prior approval of RBI**:
 - a. Private **visits** to any country (**except Nepal and Bhutan**)
 - b. **Gift** or **donation**
 - c. Going abroad for **employment**
 - d. **Emigration** (permanently settling in a country)
 - e. Maintenance of close **relatives** abroad
 - f. **Travel** for:

business

attending a
conference

specialized
training

for meeting expense of medical treatment/
check up abroad or accompanying a patient

- g. Expenses in connection with **medical treatment** abroad
- h. **Studies** abroad
- i. Any other current account transaction

Provided, for (d), (g) and (h), individual may avail forex facility > \$2,50,000 if it so required by country of emigration, medical institute offering treatment or the university, respectively

Provided further that, where **individual "Remits" any** amount under this scheme in a **FY**, the applicable limit shall be **reduced from \$250K** by such amount remitted (**i.e., the limit of \$250,000 is aggregate in FY**)

Provided also that for a **PRI but not permanently** resident in India and

- a. is a **citizen** of a foreign State other than Pakistan; or
- b. is a citizen of India, who is on **deputation (to India)** to the office or branch of a foreign co. or subsidiary or JV in India of such foreign co.,
may make remittance up to his **net salary** (after deduction of taxes, PF, etc.)

Explanation: For this schedule, a PRI on account of his employment or deputation of a specified duration (irrespective of length thereof) or for a specific job or assignments, the duration of which is not > 3 years, is a resident but not permanently resident.

2. Facilities for person other than individuals: Following shall require **prior permission** of RBI:

| Particulars | Purpose | Limit |
|------------------------------|--|--|
| Donation | Donation for: a. creation of Chairs in reputed edu. Inst., b. contribution to funds (not being an invst. fund) promoted by educational Inst; and c. contribution to a technical inst./body in the field of activity of the donor co | > Lower of 1% of Forex Earnings during last 3 FY or \$5Mn |
| Sale of flats/plots in India | Commission (per transaction) to agent abroad for sale of residential flats or commercial plots in India | > Higher of \$25,000 or 5% of Inward Remittance |
| Consultancy per project | Remittance for any consultancy w.r.t Infra projects and | > \$10Mn per project |
| Consultancy per project | For other consultancy procured from o/s India | > \$1 Mn per project |
| Pre-incorp expense | Remittance as reimbursement of pre-incorporation expense | > Higher of 5% of Investment brought into India or \$100K |

Note - Limit of \$250,000 is irrelevant in case of person other than individuals

Additional Note:

1. Procedure for Drawal/remittance of Forex under Sch III shall be same as LRS
2. Approval for transaction under Sch II and III shall **not be required** where remittance is from:
 - a) **Resident** Foreign Currency Account
 - b) **Exchange Earners'** Foreign Currency A/C (except for remittance for membership of P&I club under Sch II and payment commission/pre-incorp under Sch III)
3. If a person is **on visit abroad**, he can incur expenditure stated in **Sch III** if he incurs it through **International Credit Card** (to the extent of limit on the card)

Note - If a transaction is not listed in any of the three schedule, it can be freely undertaken.

**CAPITAL ACCOUNT TRANSACTION (SEC 6)**

Capital Account Transaction [Sec 2(e)]: means a transaction which **alters**:

- a. Asset or Liabilities (**incl. contingent liability**) o/s India of PRI
- b. Asset/Liability in India of PROI
- c. ~~Includes transaction referred u/s 6(3)~~

1. Subject to (2), a person may sell or draw forex to/from AP for CAT
2. RBI (+CG) specify:
 - Class of CAT - **involving Debt** instruments, which is **permissible**
 - Limits for such permissible transactions
 - **Conditions** placed on such transactions

Provided that, RBI or CG shall not impose restriction on drawal of forex for:

- Payment due on account of **amortization** of loans or **repayment** of loans
- **Depreciation** of direct investment in OCOB

Subsection (2A):

CG (+RBI) specify:

Class of CAT - **Not involving debt** instruments, which is **permissible**

- **Limits** for such permissible transactions
- **Conditions** placed on such transactions

3. Omitted

4. PRI may hold, own, transfer or invest in:

Foreign Currency

Foreign Security

Immovable Property Outside India

Provided that it was

- **acquired**, held or owned by such person when he was **PROI**, or
- **inherited** from a **PROI**

As per RBI Clarification:

The following transaction are covered u/s 6(4):

1. **FC accounts** opened and maintained by PRI when he was PROI
2. **Income** from employment/business/vocation when o/s India taken up when he was **PROI**, or from investment when he was PROI or from **gift/inheritance** received when he was PROI
3. Forex held o/s India by a PRI acquired by way of **inheritance** from **PROI**
4. PRI may freely **utilize eligible assets** abroad or income/sales proceed therefrom after their return to India for making payment/fresh investments abroad **without approval of RBI**.
Provided that, cost of investments is met completely out of eligible assets.

5. **PROI** may hold, own, transfer or invest in:

Indian Currency

Indian Security

Immovable Property in India

Provided that it was

- **acquired**, held or owned by such person when he was **PRI**, or
- **inherited** from a **PRI (not PROI)**

6. RBI may impose restrictions on BOA of PROI

7. Debt instrument means such instrument as determined by CG (+RBI) [**Amendment**]

CAT is broadly split into following categories as per **FEM (Permissible CAT) Regulations 2000:**

Permissible
Transaction for
PRI [Schedule I]

Permissible
Transaction for PROI
[Schedule II]

Transactions on which
restriction **cannot** be imposed
(**amortisation and depreciation**)

Prohibited
CAT



Permissible Transaction for PRI [Schedule I]

[SL-AP CG in CID style that O2 kamm pad jaye]

| | | | |
|--|---|---|--|
| Investment by PRI in ForSe | FC Loans raised in India and abroad by a PRI | Acq. Transfer of IP o/s India by a PRI | Guarantees issued by a PRI in favour of a PROI |
| Loans and Overdrafts (borrowings) by a PRI <u>from</u> a PROI | Export, import and holding of Currency /currency notes | Maintenance of FC Accounts in India and o/s India by a PRI | Taking out of Insurance policy by a PRI from an insurance co. outside India |
| Loans and Overdrafts by a PRI <u>to</u> a PROI | Remittance outside India of Capital assets of a PRI | Undertake Derivative contracts | |

Note - PRI may draw forex **not > \$250k** per FY or such amt as decided by RBI for CAT in **Sch I**

Note - Drawal of forex as per Sch III (Facilities for individual) of FEM(CUAT) Rules, 2000 shall be **subsumed** within the above limit. (i.e., Sch I + Sch III = Max \$250K)

Provided further that no part of the forex of \$ 250,000 drawn above shall be used for remittance to **non-co-operative countries** and territories (notified by Financial Action Task Force (FATF))



Permissible Transaction for PROI [Schedule II]

[IPC ke baad GD doge to Achi Co. Degi offer]

| | | | |
|---|--|--|---|
| Investment in India by a PROI, i.e., ➤ issue of security by a BC/entity in India and investment therein by PROI ➤ investment by a PROI to the capital of a firm/proprietorship concern/AOP in India. | Acquisition and transfer of IP in India by a PROI | EXIM of Currency /currency notes into/from India by a PROI. | Guarantee by a PROI in favour of a PRI |
| Deposits between a PRI and a PROI. | FC Accounts in India of a PROI | Remittance o/s India of Capital assets in India of a PROI | Undertake Derivative contract |



Prohibited CAT [Regulation 4]:

- No PROI shall make **investment** in India in any co/partnership firm/proprietary or any entity which is engaged or proposes to engage [**CARTN**]:

| | | | | | |
|---|----------------------|--|-----------------------------|------------------------------------|------------------------|
| in the business of Chit fund, or | Nidhi Company | agricultural or plantation activities | real estate business | construction of farm houses | trading in TDRs |
|---|----------------------|--|-----------------------------|------------------------------------|------------------------|

Explanation:

For the purpose of this regulation, 'real estate business' shall not include:

development of
townships,

construction of residential/commercial
premises, roads or bridges and

registered
REITs.

Note - PROIs are restricted from investment in business of Chit Funds but may be eligible to subscribe to such chits provided approval of Registrar of chits or officer of SG concerned is sought and in compliance with RBI T&Cs

2. No PRI shall undertake any CAT with a citizen/ resident/entity of Democratic People's Republic of Korea ("North Korea"), unless approval from CG
3. Any existing investment transactions with North Korea by a PRI shall be liquidated/settled within 180 days from the date of issue of this Notification, unless there is specific approval from the CG to continue beyond that period



—→... The End ...←—