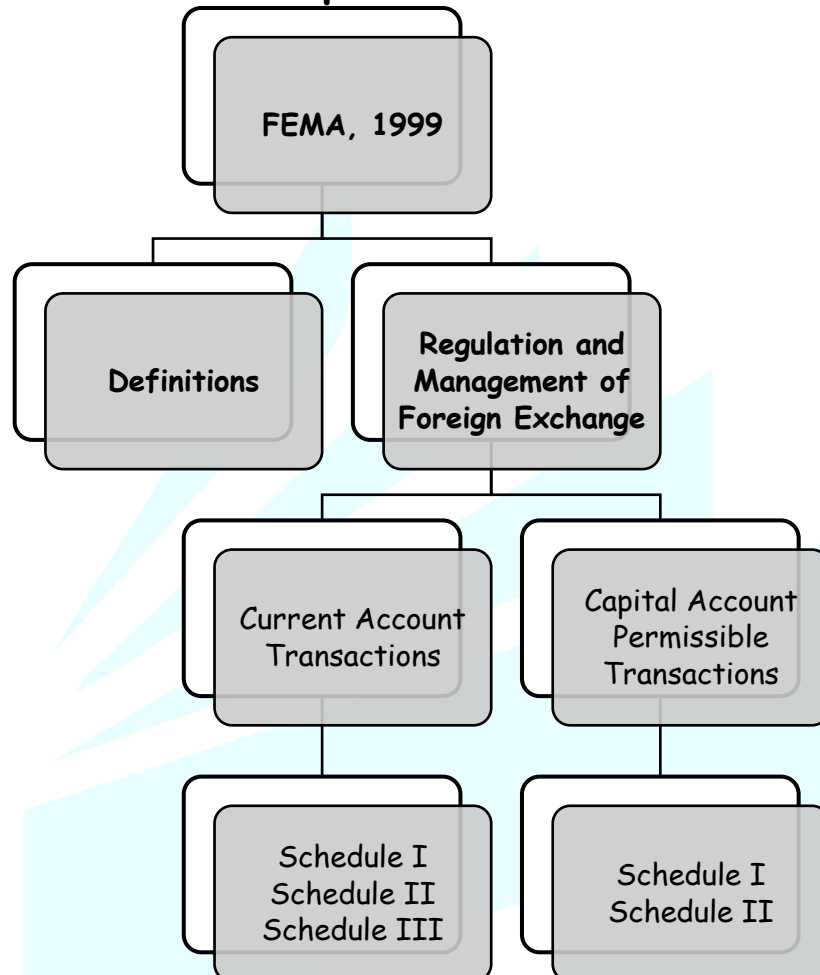


Chapter 3: The Foreign Exchange Management Act, 1999

Chapter Overview



Introduction

Need for the Act: To facilitate cross border trade and cross border capital flows, exchange control law was required. Foreign exchange control led to the introduction of exchange control law through Defence of India rules by the Britishers in 1939.

Subsequently, Foreign Exchange Regulation Act (FERA) was enacted in 1947 which was later replaced with 'the Foreign Exchange Regulation Act, 1973' (FERA).

Government as part of its agenda of liberalization of the Indian economy in 1991, permitted free movement of foreign exchange in connection to trade related receipts and payments as well as Foreign Investment in various sectors. This increased the flow of foreign exchange to India and consequently foreign exchange reserves increased substantially. The Foreign Exchange



Management Act, 1999 was **enacted and made effective from 1st June, 2000**. This Act enables management of foreign exchange reserves for the country.

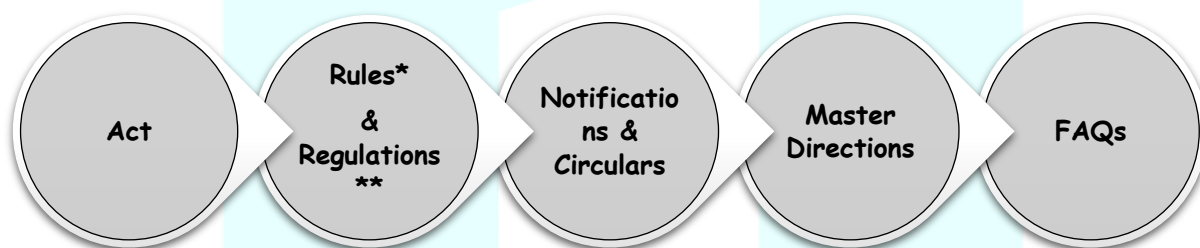
Salient Features of the Act

It provides for-

- ❖ Regulation of transactions between residents and non-residents
- ❖ Investments in India by non-residents and overseas investments by Indian residents
- ❖ Freely permissible transactions on current account subject to reasonable restrictions that may be imposed
- ❖ Reserve Bank of India (RBI) and Central Government control over capital account transactions
- ❖ Requirement for realization of export proceeds and repatriation to India
- ❖ Dealing in foreign exchange through 'Authorized Persons' like Authorized Dealer/ Money Changer/ Off-shore banking unit
- ❖ Adjudication and Compounding of Offences
- ❖ Investigation of offenses by Directorate of Enforcement
- ❖ Appeal provisions including Special Director (Appeals) and Appellate Tribunal.

Enforcement of FEMA: Though RBI exercises overall control over foreign exchange transactions, enforcement of FEMA has been entrusted to a separate 'Directorate of Enforcement' formed for this purpose. **[Section 36]**.

How to Read FEMA:



*Rules are notified by the Ministry of Finance, Government of India

** Regulations are notified by the Reserve Bank of India



Broad Structure of FEMA

Now let us have a glance at the broad structure of the Act. The Act **consists of 7 Chapters** dealing with following areas:

Chapters	Matters	Sections
I	Preliminary	1-2
II	Regulation and Management of Foreign Exchange	3-9
III	Authorized Person	10-12
IV	Contravention and Penalties	13-15
V	Adjudication and Appeal	16-35
VI	Directorate of Enforcement	36-38
VII	Miscellaneous	39-49

Preamble, Extent, Application & Commencement of FEMA, 1999

(A) Preamble	This Act aims to consolidate and amend the law relating to foreign exchange with the <u>objective of</u> - (i) facilitating external trade and payments and (i) for promoting the orderly development and maintenance of foreign exchange market in India.
(B) Extent and Application [Section 11]	FEMA, 1999 extends to the whole of India in addition, it shall also apply to all branches, offices and agencies outside India owned or controlled by a person resident in India and also to any contravention thereunder committed outside India by any person to whom this Act applies. The scope of the Act has been extended to include branches, offices and agencies outside India. The scope is thus wide enough because the emphasis is on the words " Owned or Controlled ". Contravention of the FEMA committed outside India by a person to whom this Act applies will also be covered by FEMA.
(C) Commencement	The Act, 1999 came into force with effect from 1 st June, 2000 vide Notification G.S.R. 371(E), dated 1.5.2000.

Definitions [Section 2]

In this Act, unless the context otherwise requires:

"Authorized person" [Section 2(c)]	<u>means</u> an authorized dealer, money changer, off-share banking unit or any other person for the time being authorized under section 10(1) to deal in foreign exchange or foreign securities.
"Capital Account	<u>means</u> a transaction, which alters the assets or liabilities,



"Transaction" [Section 2(e)]	including contingent liabilities, outside India of persons resident in India or assets or liability in India of persons resident outside India, and includes transactions referred to in ' Section 6(3)
"Currency" [Section 2(h)]	<u>includes</u> all currency notes, postal notes, postal orders, money orders, cheques, drafts, travellers' cheques, letters of credit, bills of exchange and promissory notes, credit cards or such other similar instruments, as may be notified by the Reserve Bank.
"Currency Notes" [Section 2(i)]	<u>means and includes</u> cash in the form of coins and banknotes
"Current Account Transaction" [Section 2(j)]	<u>means</u> a transaction other than a capital account transaction and without prejudice to the generality of the foregoing such transaction <u>includes</u> , (i) payments due in connection with foreign trade, other current business, services, and short-term banking and credit facilities in the ordinary course of business. (ii) payments due as interest on loans and as net income from investments. (iii) remittances for living expenses of parents, spouse and children residing abroad, and (iv) expenses in connection with foreign travel, education and medical care of parents, spouse and children
"Export" [Section 2(i)]	with its grammatical variations and cognate expressions <u>means</u> , (i) the taking out of India to a place outside India any goods. (ii) provision of services from India to any person outside India
"Foreign Currency" [Section 2(m)]	<u>means</u> any currency other than Indian currency.
"Foreign Exchange" [Section 2(n)]	<u>means</u> foreign currency and <u>includes</u> : (i) deposits, credits and balances payable in any foreign currency (ii) drafts, travellers' cheques, letters of credit or bills of exchange, expressed or drawn in Indian currency but payable in any foreign currency . (iii) drafts, travellers' cheques, letters of credit or bills of exchange drawn by banks, institutions or persons outside India, but payable in Indian currency .
"Foreign Security" [Section 2(o)]	<u>means</u> any security, in the form of shares, stocks, bonds, debentures or any other instrument denominated or expressed in foreign currency and includes securities expressed in foreign currency, but were redemption or any form of



	return such as interest or dividends is payable in Indian currency
"Import" [Section 2(p)]	with its grammatical variations and cognate expressions, <u>means</u> bringing into India any goods or services
"Person" [Section 2(u)]	<u>includes:</u> (i) an individual, (ii) a Hindu undivided family. (iii) a company, (iv) a firm, (v) an association of persons or a body of individuals, whether incorporated or not, (vi) every artificial juridical person, not falling within any of the preceding sub-clauses, and; (vii) any agency, office or branch owned or controlled by such person
"Person resident in India" [Section 2(v)]	<u>means:</u> (i) a person residing in India for more than 182 days during the course of the preceding financial year but does not include- (A) a person who has gone out of India or who stays outside India, in either case- (a) for or on taking up employment outside India, or (b) for carrying on outside India a business or vocation outside India, or (c) for any other purpose, in such circumstances as would indicate his intention to stay outside India for an uncertain period: (B) a person who has come to or stays in India, in either case, otherwise than (a) for or on taking up employment in India, or (b) for carrying on in India a business or vocation in India, or (c) for any other purpose, in such circumstances as would indicate his intention to stay in India for an uncertain period: (ii) any person or body corporate registered or incorporated in India, (iii) an office, branch or agency in India owned or controlled by a person resident outside India, (iv) an office, branch or agency outside India owned or controlled by a person resident in India
"Person Resident Outside India" [Section 2(w)]	<u>means</u> a person who is not resident in India.



'Transfer" [Section 2(ze)]	includes sale, purchase, exchange, mortgage, pledge, gift, loan or any other form of transfer of right, title, possession or lien.
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Residential Status under FEMA, 1999

► The definition of "person" is similar to the definition contained in the Income-tax Act, 1961.

► The term 'person' includes entities such as companies, firms, individuals, HUF, Association of Persons (AOP), artificial juridical persons agencies, as well as offices and branches.

Agencies, offices and branches do not have independent status separates from their owners. Yet these have been considered as persons. Under FEMA such offices and

branches are included in the definition of Person Resident in India. Therefore, they have been included in the definition of "Person".

► The term 'person resident in India' means the following entities:

1. A person who resides in India for more than 182 days during the preceding financial year;

The following persons are NOT persons resident in India even though they may have resided in India for more than 182 days.

A. A person who has gone out of India or stays outside India for any of the three purposes given below,

B. A person who has come to or stays in India OTHERWISE THAN for any of the three purposes given below;

Three Purposes

(1) For or on taking up Employment

(ii) For carrying on a business or Vacation

(iii) For any other purpose in such circumstances as would indicate stay for an uncertain period.

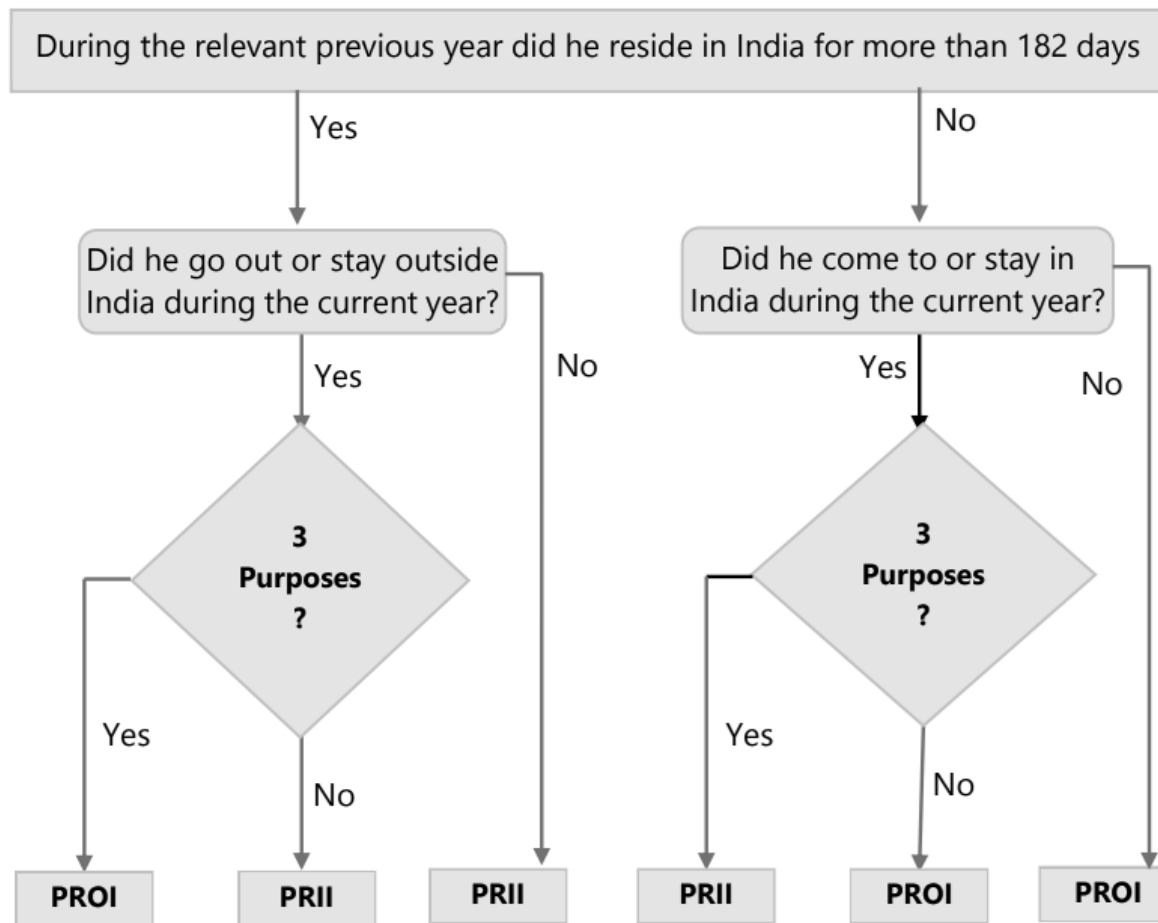
2. Any person or body corporate registered or incorporated in India;

3. An office, branch or agency in India owned or controlled by a person resident outside India

4. An office, branch or agency outside India owned or controlled by a person resident in India.



Person resident outside India means a person who is **not** resident in India.



As the definitions of Person Resident in India (PRII) and Person Resident outside India (PROI) are quite relevant for determining the applicability of the Act on an entity, let us analyse and understand it better.

In the case of individuals, to be considered as "resident", the person should have resided in India in the preceding financial year for more than 182 days. Citizenship is not the criteria for determining whether or not a person is resident in India.

There are three limbs in the definition.

The first limb prescribes the number of days stay. Then there are two limbs which are exceptions to the first limb.

First limb - It states that a person who is in India for more than 182 days in the "preceding year" will be a Person Resident in India. Thus, at the threshold or basic level, one has to consider the period of stay during the preceding year.



Example: If a person resides in India for more than 182 days during FY 2020-21, then for FY 2021-22, the person will be an Indian resident. For FY 2020-21, one will have to consider residence during FY 2019-20, and so on.

There are two exceptions provided in clauses (A) and (B).

- ▶ **Clause (A)** is for persons going out of India.
- ▶ **Clause (B)** is for persons coming into India.

Exceptions carve out situations that **do not fall** under the main body of a section, **even though they satisfy the criteria**. This means that even if a person is an Indian resident based on the test provided in the first limb, the person will be a **"Person Resident Outside India (PROI)** if he falls within limb (A) or limb (B).

Clause (A) - second limb - It states that if a person leaves India in any of the THREE PURPOSES we saw above, he will not be a PRII. He will be a PROI

Example given for the first limb above, if a person leaves India on 1st November 2021, he will be a non-resident from 2nd November 2021 - even though his number of days in India was more than 182 days in FY 2020-2021.

Similarly, if a person goes and stays out of India for carrying on any business, he will be a PROI from that date, For FY 2021-2022 the person will be a PRII till 1st November 2021. He will then be a PROI. From 1 April 2022, the person will continue to be a PROI as long as he stays out of India for employment.

An **example** for clause (iii) can be a person who has a **green card in the USA**. The green card entitles a person to stay in the USA and eventually become a US citizen. If **a person goes abroad and starts staying in the USA**, he will be a non-resident from that date as his stay abroad indicates that he is going to stay there for an uncertain period.

Clause (B) - Third limb - This is a complex clause as the first limb read with the third limb has two exceptions. Limb, one uses the phrase **"but does not include"**. Third limb uses the phrase **"otherwise than"**. Use of two exceptions makes it complex reading.

It states that if a person has come to India **for any reason otherwise than** for employment, business or circumstances which indicate his intention to stay for an uncertain period - he will be a non-resident. This will be so even if the person has stayed in India for **more than 182 days in the preceding year**.



Example: if a person comes to India on 1 June 2021 to visit his parents. However, his parents fall sick and he stays till 31 March 2022. Thereafter he continues to stay in India. It is however certain that he will leave India in the next 6 months when his parents recover. His stay in India is neither for employment, nor for business, nor for circumstances which show that he will stay in India for an uncertain period. In such a case, even if he has resided in India for more than 182 days in FY 2021-2022, he will continue to be a non-resident from 1st April 2022 also. In FY 2021-2022, he is of course a PROI as he did not reside in India for more than 182 in FY 2020-2021.

If a person comes to India on 1st June 2021 for employment, business or circumstances which indicate his intention to stay in India for an uncertain period, he will be a PRII from 1st June 2021.

Authors Note: Residential status is not for a year. It is from a particular date. This is different from income-tax law. Under income-tax law, a person has to pay tax in respect of the income of the previous year. Therefore, it is possible to look at a complete year for determining residential status under the Income Tax Act, 1961. FEMA is a regulatory law. One has to know the person's status at the time of undertaking a transaction.

Example, a person comes to India for employment, and if his status can be known only when the year is completed, how will he and other people enter into commercial transactions with each other? If he is considered as a PROI till the year is over, then people will not be able to enter into transactions with him. This is the reason why the residential status is not for a year but from a particular date.

It is understood that this condition applies only to individuals. It will not apply to HUF, AOP or artificial juridical persons as they cannot get employed, cannot go out of India or come to India. Hence, they do not come within the ambit of the second and third limbs. These entities like HUF and AOP are not required to be registered or incorporated like corporate entities nor the definition can be far stretched to cover by applying the criteria of 'owned or controlled'. Hence legally the definition for HUF, AOP, BOI fails. Practically if the HUF, AOP etc. are in India, they will be considered as Indian residents.

Person or Body corporate: Any person or body corporate registered or incorporated in India, will be considered a PRII. This definition too, does not apply to AOP, BOI etc.



Office, branch or agency: Any agency, branch or agency outside India but **owned or controlled by PRII** will be considered as a person resident in India (PRII). Thus, one cannot set up a branch outside India and attempt to avoid FEMA provisions.

Any agency, branch or agency in India but **owned or controlled by a person resident outside India (PROI)** will be considered as a person resident in India. This is relevant as Indian residents can deal with such branches in India without considering FEMA. If such a branch is considered as a PROI then it will be difficult to undertake several transactions.

Illustration: Mr. X had resided in India during the financial year 2019-2020 for less than 182 days. He had come to India on April 1, 2020 for carrying on business. He intends to leave the business on April 30, 2021 and leave India on June 30, 2021. Determine his residential status for the financial years 2020-2021 and 2021-2022 up to the date of his departure?

Ans- As explained in the above illustration, Mr. X will be considered as a 'person resident in India' from 1st April 2020. As regards, financial year 2021-2022, Mr. X would continue to be an Indian resident from 1st April 2021. If he leaves India for the purpose of taking up employment or for business/vocation outside India, or for any other purpose as would indicate his intention to stay outside India for an uncertain period, he would cease to be person resident in India from the date of his departure.

It may be noted that even if Mr. X is a foreign citizen, has not left India for any of these purposes, he would be considered, 'person resident in India' during the financial year 2021-2022. Thus, it is the purpose of leaving India which will decide his status from 1st July 2021.

Illustration: Mr. Z had resided in India during the financial year 2019-2020. He left India on 1st August, 2020 for United States for pursuing higher studies for three years. What would be his residential status during financial year 2020-2021 and during 2021- 2022?

Ans- Mr. Z had resided in India during financial year 2019-2020 for more than 182 days. After that he has gone to USA for higher studies. He has not gone out of or stayed outside India for or on taking up employment, or for carrying a business or for any other purpose, in circumstances as would indicate his intention to stay outside India for an uncertain period. Accordingly, he would be 'person resident in India' during the financial year 2020-2021. RBI has however clarified in its AP circular no. 45 dated 8th December 2003, that students will



be considered as non-residents. This is because usually students start working there to take care of their stay and cost of studies.

For the financial year 2021-2022, he would not have been in India in the preceding financial year (2020-2021) for a period exceeding 182 days. Accordingly, he would not be 'person resident in India' during the financial year 2021-2022.

Illustration: Toy Ltd. is a Japanese company having several business units all over the world. It has a robotic unit with its headquarters in Mumbai and has a branch in Singapore. The Headquarters at Mumbai controls the Singapore branch of the robotic unit. What would be the residential status of the robotic unit in Mumbai and that of the Singapore branch?

Ans- Toy Ltd. being a Japanese company would be a person resident outside India. [Section 2(w)]. Section 2(u) defines 'person'. Under clause (viii) thereof person would include any agency, office or branch owned or controlled by such 'person'. The term such 'person' appears to refer to a person who is included in clauses (i) to (vi). Accordingly, robotic unit in Mumbai, being a branch of a company, would be a 'person'.

Section 2(v) defines 'person resident in India'. Under clause (iii) thereof 'person resident in India' would include an office, branch or agency in India owned or controlled by a person resident outside India. Robotic unit in Mumbai is owned or controlled by a person 'resident outside India'. Hence, it would be 'person resident in India'.

The robotic unit headquartered in Mumbai, which is a person resident in India as discussed above, controls the Singapore branch, Hence, the Singapore branch is a 'person resident in India'.

Illustration: Miss Alia is an airhostess with the British Airways. She flies for 12 days in a month and thereafter takes a break for 18 days. During the break, she is accommodated in 'base', which is normally the city where the Airline is headquartered. However, for security considerations, she was based at Mumbai. During the financial year, she was accommodated at Mumbai for more than 182 days. What would be her residential status under FEMA?

Ans- Miss Alia stayed in India at Mumbai 'base' for more than 182 days in the preceding financial year. She is however employed in UK. She has not come to India for employment, business or circumstances which indicate her intention to stay for uncertain period. Under section 2(v)(B), such persons are not considered as Indian residents even if their stay exceeds 182 days in the



preceding year. Thus, while Miss Alia may have stayed in India for more than 182 days, she cannot be considered to be a Person Resident in India.

If, however she has been employed in Mumbai branch of British Airways, then she will be considered a Person Resident in India.

Regulation and Foreign Exchange

Dealing in foreign exchange, etc.(Section 3)

No person shall-

- (a) deal in or transfer any foreign exchange or foreign security to any person not being an authorized person (AP);
- (b) make any payment to or for the credit of any person resident outside India in any manner;
- (c) receive otherwise than through an authorized person, any payment by order or on behalf of any person resident outside India in any manner.

Explanation For the purpose of this clause, where any person in, or resident in, India receives any payment by order or on behalf of any person resident outside India through any other person (including an authorized person) without a corresponding inward remittance from any place outside India, then, such person shall be deemed to have received such payment otherwise than through an authorized person;

(d) enter into any financial transaction in India as consideration for or in association with acquisition or creation or transfer of a right to acquire any asset outside India by any person.

The above transactions may carry on:

- (a) as otherwise provided in this Act; or
- (b) with the general or special permission of the Reserve Bank.

Explanation For the purpose of this clause, "**financial transaction**" **means** making any payment to, or for the credit of any person, or receiving any payment for, by order or on behalf of any person, or drawing, issuing or negotiating any bill of exchange or promissory note, or transferring any security or acknowledging any debt.

This section imposes blanket restrictions on the specified transactions. This section applies to PRIIs and PROIS. The purpose of this section is to regulate inflow and outflow of Foreign Exchange through Authorized dealers and in a permitted manner.

Consider following examples:

(i) Example pertaining to clause (a)- Dealing in foreign exchange - A PROI comes to India and would like to sell US\$ 1,000 to his friend who is resident in



India. The friend offers him a rate better than the banks. This cannot be done as it would amount to dealing in foreign exchange.

(ii) Example pertaining to clause (b) - A PROI has an insurance policy in India. He requests his brother in India to pay the insurance premium. This will amount to payment for the credit of non-resident. This is not permitted.

(iii) Example pertaining to clause (c)- A foreign tourist comes to India and he takes food at a restaurant. He would like to pay US\$ 20 in cash to the restaurant. The restaurant cannot accept cash as it will be a receipt otherwise than through an Authorized Person. The restaurant will have to take a money changers license to accept foreign currency.

(iv) Examples pertaining to clause (d)- Transactions covered by this subsection are known as Hawala transactions. An Indian resident gives 770,000 in cash to an Indian dealer. For this transaction, the brother in Dubai will get US\$ 1,000 from a Dubai dealer. The two dealers may settle the transactions later. However, transaction is not permitted

Holding of foreign exchange (Section 4)

Except as provided in this Act, no person resident in India shall acquire, hold, own, possess or transfer any foreign exchange, foreign security or any immovable property situated outside India.

This section prevents Indian residents from acquiring, holding, owning, possessing or transferring any foreign exchange, foreign security or immovable property abroad. Then through separate notifications, acquisition of these assets has been permitted

subject to certain conditions and compliance rules.

Example: If an Indian resident receives a bank balance of US\$ 10,000 from his uncle in London, the Indian resident cannot hold on to the foreign funds. He is supposed to bring back the funds as provided in section 8.

Current account transactions (Section 5)

The term '**Current Account Transaction is defined negatively by Section 20**) of the Act. It means a transaction **other than a capital account transaction and includes the following types of transactions:**

- (i) Payments in the course of ordinary course of foreign trade, other services such as short-term banking and credit facilities in the ordinary course of business etc.
- (ii) Payments in the form of interest on loans or income from investments.
- (iii) Remittances for living expenses of parents, spouse, or children living abroad
- (iv) Expenses in connection with foreign travel, education etc.



Example: An Indian resident imports machinery from a vendor in the UK for installation in his factory. As per accounts and income-tax law, machinery is a "capital expenditure". However, under FEMA, it does not alter (create) an asset in India for the UK vendor. It does not create any liability to a UK vendor for the Indian importer. Once the payment is made, the Indian resident or the UK vendor neither owns nor is owed anything in the other country. Hence it is a Current Account Transaction.

If a gift is a current account transaction, why is there a restriction under Current Account regulations?

It is because while there is no restriction on Current Account transactions, some reasonable restrictions can be imposed. Otherwise, people may transfer funds abroad under the garb of current account transactions.

If, however the PRII gives a PROI a gift in India in Indian currency, for the PROI it will result in funds lying in India (alteration of Indian asset). For PRII, there is no creation of asset or a liability. As this transaction creates an asset in India for the PROI, it is a Capital Account transaction.

In a similar manner, if a PROI gives a gift to a PRII by remitting funds in India, there is no restriction. However, if the PROI gives the funds abroad, the resident cannot keep it abroad. He has to bring it to India.

Any person may sell or draw foreign exchange to or from an authorized person if such sale or draw is a current account transaction.

The Central Government may, in public interest and in consultation with the Reserve Bank, impose such **reasonable restrictions** for current account transactions as prescribed under the FEM (Current Account Transactions) Rules, 2000.

The general rule to be understood is that Current Account transactions are freely permitted unless specifically prohibited and Capital Account transactions are prohibited unless specifically or generally permitted.

Section 5 of the Act permits any person to sell or draw Foreign Exchange to or from an Authorized person to undertake any current account transaction. The Central Government has the power to impose reasonable restrictions, in consultation with the RBI and in public interest on current account transactions. The Central Government has in exercise of this power issued the Foreign Exchange Management (Current Account Transactions) Rules, 2000.

Let us now see the various schedules to the Rules that lay down the restrictions:

SCHEDULE-I

Transactions for which draw of **foreign exchange is prohibited:**

- (i) Remittance out of lottery winnings.
- (ii) Remittance of income from racing/riding, etc., or any other hobby.
- (iii) Remittance for purchase of lottery tickets, banned/prescribed magazines, football pools, sweepstakes etc.
- (iv) Payment of commission on exports made towards equity investment in Joint Ventures/Wholly Owned Subsidiaries abroad of Indian companies.
- (v) Remittance of dividend by any company to which the requirement of dividend balancing is applicable.
- (vi) Payment of commission on exports under Rupee State Credit Route, except **commission up to 10% of invoice value of exports of tea and tobacco.**
- (vii) Payment related to **"Call Back Services"** of telephones.
- (viii) Remittance of interest income on funds held in **Non-resident Special Rupee Scheme a/c.**

SCHEDULE-II

Transactions, which require prior approval of the Government of India for draw of foreign exchange:

Purpose of Remittance	Ministry/Department of Govt. of India whose approval is required
Cultural Tours	Ministry of Human Resources Development (Department of Education and Culture)
Advertisement in foreign print media for the purposes other than promotion of tourism, foreign investments and international bidding (exceeding US\$ 10,000) by a State Government and its Public Sector Undertakings.	Ministry of Finance, Department of Economic Affairs
Remittance of freight of vessel chartered by a PSU	Ministry of Surface Transport (Chartering Wing)
Payment of import through ocean transport by a Govt. Department or a PSU on c.i.f. basis (ie., other than f.o.b. and f.a.s. basis)	Ministry of Surface Transport (Chartering Wing)
Multi-modal transport operators making remittance to their agents abroad	Registration Certificate from the Director General of



	Shipping
Remittance of hiring charges of transponders by (a) TV Channels (b) Internet service providers	Ministry of Information and Broadcasting Ministry of Communication and Information Technology.
Remittance of container detention charges exceeding 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 amount involved exceeds US \$100,000	Ministry of Human Resource Development (Department of Youth Affairs and Sports)
Remittance for membership of P & I Club	Ministry of Finance (Insurance Division)

Transactions which require RBI's prior approval for draw of foreign exchange:

SCHEDULE-III

1. Facilities for individuals- Individuals can avail of foreign exchange facility for the following purposes **within the limit of USD 250,000 only.:**

- (i) Private visits to any country (except Nepal and Bhutan)
- (ii) Gift or donation.
- (iii) Going abroad for employment
- (iv) Emigration
- (v) Maintenance of close relatives abroad
- (vi) Travel for business or attending a conference or specialized training or for meeting expenses for meeting medical expenses, or check-up abroad, or for accompanying as attendant to a patient going abroad for medical treatment/ check-up.
- (vii) Expenses in connection with medical treatment abroad
- (viii) Studies abroad
- (ix) Any other current account transaction

Any additional remittance in excess of the said limit for the said purposes shall require **prior approval of the Reserve Bank of India.**

However, for the purposes mentioned at item numbers (iv), (vii) and (viii) above, the individual may avail of exchange facility for an amount in excess of the limit prescribed under the Liberalised Remittance Scheme as provided in regulation 4 to FEMA Notification 1/2000-RB, dated the 3rd May, 2000 (here in after



referred to as the said Liberalized Remittance Scheme) if it is so required by a country of emigration, medical institute offering treatment or the university, respectively:

Further, if an individual remits any amount under the said Liberalized Remittance Scheme in a financial year, then the applicable limit for such individual would be reduced from **USD 250,000 (US Dollars Two Hundred and Fifty Thousand Only)** by the amount so remitted:

Further, that for a person who is resident 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 the office or branch of a foreign company or subsidiary or joint venture in India of such foreign Company may make remittance up to his net salary (after deduction of taxes, contribution to provident fund and other deductions).

Explanation: For the purpose of this item, a person resident in India 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 does not exceed three years, is a resident but not permanently resident:

Further, a person other than an individual may also avail of foreign exchange facility, **mutatis mutandis, within the limit** prescribed under the said Liberalized Remittance Scheme for the purposes mentioned herein above.

2. Facilities for persons other than individual-The following remittances by persons other than individuals shall require prior approval of the Reserve Bank of India:

- (i) Donations exceeding one per cent. of their foreign exchange earnings during the **previous three financial years or USD 5,000,000, whichever is less**, for-
 - a. creation of Chairs in reputed educational institutes,
 - b. contribution to funds (not being an investment fund) promoted by educational institutes; **and**
 - c. contribution to a technical institution or body or association in the field of activity of the donor Company.

- (ii) Commission, per transaction, to agents abroad for sale of residential flats or commercial plots in India **exceeding USD 25,000 or five percent of the inward remittance whichever is more.**



(iii) Remittances **exceeding USD 10,000,000** per project for any consultancy services in respect of infrastructure projects **and USD 1,000,000 per project**, for other consultancy services procured **from outside India**.

Explanation-For the purposes of this sub-paragraph, the expression "infrastructure" shall mean as defined in explanation to para 1(iv)(A)(a) of Schedule I of FEMA Notification 3/2000-RB, dated May 3, 2000.

(iv) Remittances **exceeding five per cent of investment brought into India or USD 100,000 whichever is higher**, by an entity in India by way of reimbursement of pre-incorporation expenses.

3. Procedure-The procedure for draw or remittance of any foreign exchange under this schedule shall be the same as applicable for remitting any amount under the said Liberalized Remittance Scheme.

If the transaction is not listed in any of the above three schedules, it can be freely undertaken.

Exemption for remittance from RFC Account - **No approval** is required where any remittance has to be made for the transactions listed in Schedule II and Schedule III above from a **Resident Foreign Currency (RFC) account**.

Exemption for remittance from EEFC Account - If any remittance has to be made for the transactions listed in Schedule II and Schedule III above from **Exchange Earners' Foreign Currency (EEFC) account**, then also no approval is required. However, if payment has to be made for the following transactions, approval is required even if payment is from EEFC account:

- Remittance for membership of P & I Club.
- Commission, per transaction, to agents abroad for sale of residential flats or commercial plots in India exceeding USD 25,000 or five per cent of the inward remittance whichever is more. Remittances **exceeding five per cent of investment brought into India or USD 100,000 whichever is higher**, by an entity in India by way of reimbursement of pre-incorporation expenses.

Exemption for payment by International Credit Card while on a visit abroad

If a person is on a visit abroad, he can incur expenditure stated in Schedule III if he incurs it through international credit card.

Note:

Liberalized Remittance Scheme (LRS): Under the Liberalised Remittance Scheme (LRS), all resident individuals, including minors, are allowed to freely remit up to USD 250,000 per financial year (April - March) for any permissible



current or capital account transaction or a combination of both. This is inclusive of foreign exchange facility for the purposes mentioned in Para 1 of Schedule III of Foreign Exchange Management (CAT) Amendment Rules 2015, dated May 26, 2015.

In case of remitter being a minor, the LRS declaration form must be countersigned by the minor's natural guardian. The Scheme is not available to corporates, partnership firms, HUF, Trusts etc.

Consolidation of remittance of family members Remittances under the Scheme can be consolidated in respect of family members subject to individual family members complying with its terms and conditions.

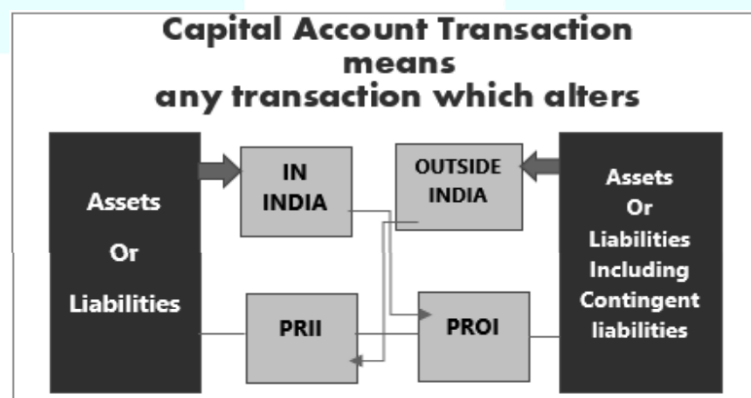
Exception: Clubbing is *not permitted* by other family members for **capital account transactions** such as opening a bank account/investment/purchase of property, if they are not the co-owners/co-partners of the overseas bank account/investment/property.

Capital account transactions (Section 6)

The definitions of "**Capital Account Transactions**" and its opposite "current account transactions" are contained in **clauses (e) and (j) of Section 2**. The regulations under FEMA apply to a transaction based on whether the transaction is a "Capital Account Transaction" or a "Current Account Transaction". These transactions broadly outline the basics and whole approach of the Act.

Basically, these two transactions have to be understood as being similar to the concepts of items relating to the profit and loss account or revenue items (with respect to current account transactions) and of Balance Sheets or capital items (with respect to capital account transactions).

Capital Account Transactions means "A transaction which alters the assets or liabilities including contingent liabilities outside India of persons resident in India or assets or liabilities in India of persons resident outside India would be a capital account transaction."



Capital Accounts Transaction in India can be carried out only to the extent permitted because Indian Rupee is not yet fully convertible. Capital and current account transactions are intended to be mutually exclusive. **A transaction which alters the asset or liabilities in India of non-residents falls under the category of capital account.** However, as far as residents are concerned **transactions which alter the contingent liabilities outside India are also capital account transactions.** The Reserve Bank of India may by regulations place restrictions on various specified capital account transactions.

In simple terms, cross border transactions pertaining to investments, loans, immovable property, transfer of assets are Capital Account Transactions

(1) Subject to the provisions of **sub-section (2)**, any person may **sell or draw foreign exchange to or from an authorized person** for a capital account transaction.

(2) Reserve Bank had the **power to specify the Capital Account transactions which are permitted and the relevant limits, terms and conditions.** By Finance Act 2015, powers for regulation of Capital Account Transactions for Non-debt instruments were transferred to the Central Government. RBI continued to have powers to regulate debt instruments. The amendments have however been made effective from 15 October 2019. Now the regulations are as under.

The Reserve Bank may, in consultation with the Central Government, specify:

- (a) any class or classes of capital account transactions, involving debt instruments, which are permissible;
- (b) the limit up to which foreign exchange shall be admissible for such transactions;
- (c) any conditions which may be placed on such transactions,

Provided that the Reserve Bank or the Central Government shall not impose any restrictions on the draw of foreign exchange for payment due on account of amortization of loans or for depreciation of direct investments in the ordinary course of business.

RBI has issued notification for Debt instruments specifying the terms and conditions. These regulations for foreign investment in debt instruments. For investment by Indian residents outside India, RBI continues to have power to regulate the transactions for equity and debt.

(2A) The Central Government may, in consultation with the Reserve Bank, prescribe



- (a) any class or classes of capital account transactions, not involving debt instruments, **which are permissible**;
- (b) the limit up to which foreign exchange shall be admissible for such transactions; and
- (c) any conditions which may be placed on such transactions.

The Central Government has issued notification for non-debt instruments specifying the terms and conditions. RBI has issued notification for mode of payment and reporting of non-debt instruments.

(3) Before 15th October 2019, **Section 6(3)** specified a list of capital account transactions which could be regulated by RBI [apart from the general powers which it had under **Section 6(2)**]. **This list has now been deleted from 15th October 2019.**

(4) A person resident in India may hold, own, transfer or invest in foreign currency, foreign security or any immovable property situated outside India if such currency, security or property was acquired, held or owned by such person **when he was resident outside India or inherited from a person who was resident outside India.**

The RBI vide A.P. (DIR Series) Circular No. 90 dated 9th January, 2014 has issued a clarification on **section 6(4)** of the Act. This circular clarifies that **section 6(4)** of the Act covers the following transactions:

- (i) Foreign currency accounts opened and maintained by such a person when he was resident outside India;
- (ii) Income earned through employment or business or vocation outside India taken up or commenced which such person was resident outside India, or from investments made while such person was resident outside India, or from gift or inheritance received while such a person was resident outside India;
- (iii) Foreign exchange **including** any income arising therefrom, and conversion or replacement or accrual to the same, held outside India by a person resident in India acquired by way of inheritance from a person resident outside India.
- (iv) A person resident in India may freely utilize all their eligible assets abroad as well as income on such assets or sale proceeds thereof received after their return to India for making any payments or to make any fresh investments abroad without approval of Reserve Bank, provided the cost of such investments and/or any subsequent payments received therefor are met exclusively out of funds forming part of eligible assets held by them and the transactions is not in contravention to extant FEMA provisions.

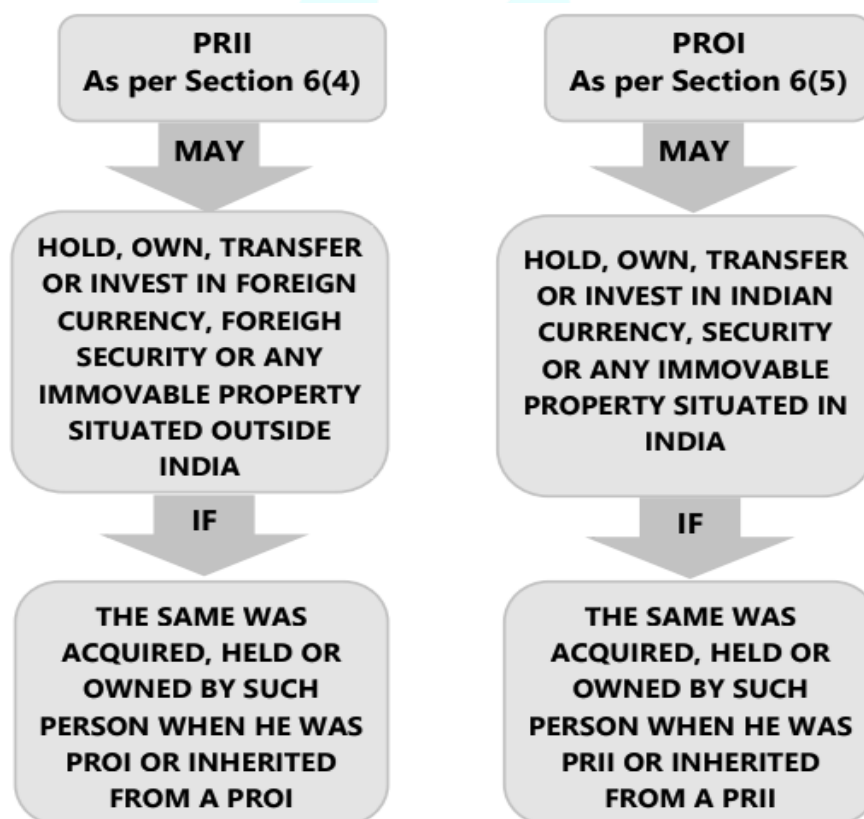
(5) A person resident outside India may hold, own, transfer or invest in Indian currency, security or any immovable property situated in India if such



currency, security or property was acquired, held or owned by a such person when he was resident in India or inherited from a person who was resident in India.

(6) Without prejudice to the provisions of this section, the Reserve Bank may, by regulation, prohibit, restrict, or regulate establishment in India of a branch, office or other place of business by a person resident outside India, for carrying on any activity relating to such branch, office or other place of business.

Capital Account Transactions [Section 6(4) & 6(5)]



(7) For the purposes of this section, the term "debt instruments" shall mean, such instruments as may be determined by the Central Government in consultation with the Reserve Bank.

A capital account transaction as stated earlier is a transaction, which alters the assets or liabilities, including contingent liabilities, outside India of persons resident in India or assets or liabilities in India of persons resident outside India would be a capital account transaction. The section gives a liberty by providing that any person may sell or draw foreign exchange to or from an authorized person for capital account transactions. However, the liberty to do so is subject to the provisions of **sub-section (2) and (2A)**, which states



that the Reserve Bank and the Central Government may specify class or classes of capital account transactions, which are permissible limit up to, which the foreign exchange shall be admissible for such transactions and the conditions which may be placed on such transactions.

Capital account transaction is basically split into the following categories under **Foreign Exchange Management (Permissible capital account transactions) Regulations, 2000-:**

- (I) transactions, which are permissible in respect of persons resident in India and outside India.
- (II) transaction on which restrictions cannot be imposed; and
- (III) transactions, which are prohibited.

I. Permissible Transactions

Under **sub-section (2) of Section 6**, the RBI has issued the Foreign Exchange Management (Permissible Capital Account Transactions) Regulations, 2000. The Regulations specify the list of transactions, which **are permissible in respect of persons resident in India in Schedule-1** and the classes of capital account transactions of **persons resident outside India in Schedule-II**.

Further, subject to the provisions of the Act or the rules or regulations or direction or orders made or issued thereunder, **any person may sell or draw foreign exchange to or from an authorized person** for a capital account transaction specified in the Schedules; provided that the transaction is within the limit, if any, specified in the regulations relevant to the transaction.

SCHEDULE-I

The list of permissible classes of transactions made by **persons resident in India** is:

- (a) Investment by a person resident in India in foreign securities.
- (b) Foreign currency loans raised in India and abroad by a person resident in India.
- (c) Transfer of immovable property outside India by a person resident in India.
- (d) Guarantees issued by a person resident in India in favour. of a person resident outside India.
- (e) Export, import and holding of currency/currency notes.
- (f) Loans and overdrafts (borrowings) by a person resident in India from a person resident outside India.
- (g) Maintenance of foreign currency accounts in India and outside India by a person resident in India.



- (h) Taking out an insurance policy by a person resident in India from an insurance company outside India.
- (i) Loans and overdrafts by a person resident in India to a person resident outside India.
- (j) Remittance outside India of capital assets of a person resident in India.
- (k) Undertake derivative contracts

SCHEDULE-II

The list of permissible classes of transactions made by **persons resident outside India** is:

- (a) Investment in India by a person resident outside India, that is to say,
 - (i) issue of security by a body corporate or an entity in India and investment therein by a person resident outside India; and
 - (ii) investment by way of contribution by a person resident outside India to the capital of a firm or a proprietorship concern or an association of a person in India.
- (b) Acquisition and transfer of immovable property in India by a person resident outside India.
- (c) Guarantee by a person resident outside India in favor of, or on behalf of, a person resident in India.
- (d) Import and export of currency/currency notes into/from India by a person resident outside India.
- (e) Deposits between a person resident in India and a person resident outside India.
- (f) Foreign currency accounts in India of a person resident outside India.
- (g) Remittance outside India of capital assets in India of a person resident outside India.
- (h) Undertake derivative contracts

Transactions with no restriction They are:

- (1) For amortization of loan and
- (2) For depreciation of direct investments in ordinary course of business. Also, restrictions cannot be imposed when draw is for the purpose of repayments of loan instalments.

Prohibited Transactions

On certain transactions, the Reserve Bank of India imposes prohibition.

- (a) no person shall **undertake or sell or draw foreign exchange to or from an authorized person** for any capital account transaction, provided that-
 - (i) subject to the provisions of the Act or the rules or regulations or directions or orders made or issued thereunder, **a resident individual may, draw from an authorized person foreign exchange not exceeding USD 250,000**



per financial year or such amount as decided by Reserve Bank from time to time for a capital account transaction specified in Schedule I.

Explanation: Draw of foreign exchange as per item number 1 of Schedule III to Foreign Exchange Management (Current Account Transactions) Rules, 2000 dated 3rd May 2000 as amended from time to time, shall be subsumed within the limit under proviso (a) above.

(ii) Where the **drawal of foreign exchange** by a resident individual for any capital account transaction specified in Schedule I **exceeds USD 250,000 per financial year, or as decided by Reserve Bank** from time to time as the case may be, the limit specified in the regulations relevant to the transaction shall apply with respect to such drawal.

Provided further that no part of the foreign exchange of USD 250,000, drawn under proviso (a) shall be used for remittance directly or indirectly to countries notified as non-co-operative countries and territories by Financial Action Task Force (FATF) from time to time and communicated by the Reserve Bank of India to all concerned.

(b) The **person resident outside India is prohibited from making investments in India** in any form, in any company, or partnership firm or proprietary concern or any entity whether incorporated or not which is engaged or proposes to engage:

(i) **In the business of chit funds;** Registrar of Chits or an officer authorized by the state government on this behalf, may, in consultation with the State Government concerned, permit any chit fund to accept subscriptions from Non-resident Indians. Non-resident Indians shall be eligible to subscribe, through banking channel and on non-repatriation basis, to such chit funds, without limit subject to the conditions stipulated by the Reserve Bank of India from time to time

(ii) **As Nidhi company;**

(iii) **In agricultural or plantation activities;**

(iv) **In real estate business, or construction of farm houses or**

Explanation: In "real estate business" the term shall not include development of townships, construction of residential/commercial premises, roads or bridges and Real Estate Investment Trusts (REITs) registered and regulated under the SEBI (REITs) Regulations 2014, or

(v) **in trading in Transferable Development Rights (TDRs).**



'Transferable Development Rights' means certificates issued in respect of category of land acquired for public purpose either by Central or State Government in consideration of surrender of land by the owner without monetary compensation, which are transferable in part or whole:

(c) **No person resident in India shall undertake** any capital account transaction which is not permissible in terms of Order S.O. 1549(E) dated April 21, 2017, as amended from time to time, of the Government of India, Ministry of External Affairs, **with any person who is, a citizen of or a resident of Democratic People's Republic of Korea, or an entity incorporated or otherwise, in Democratic People's Republic of Korea,** until further orders, unless there is specific approval from the Central Government to carry on any transaction.

(d) The **existing investment transactions, with any person who is, a citizen of or resident of Democratic People's Republic of Korea, or an entity incorporated or otherwise in Democratic People's Republic of Korea, or any existing representative office or other assets possessed in Democratic People's Republic of Korea, by a person resident in India,** which is not permissible in terms of Order S.O. 1549(E) dated April 21, 2017, as amended from time to time, of the Government of India, Ministry of External Affairs **shall be closed/liquidated/disposed/settled within a period of 180 days from the date of issue of this Notification,** unless there is specific approval from the Central Government to continue beyond that period."

Thus, a capital account transaction is permitted only if it is specifically permitted under the regulations. If the transaction is not stated as generally permitted, a prior specific approval is required.