

Overview of FEMA, Residential Status, Capital and Current Account Transactions

VIRTUAL REFRESHER COURSE ON FEMA
WIRC OF ICAI
7th May 2021

Shah & Modi

CHARTERED ACCOUNTANTS

By:
CA Manoj Shah
e-mail :manoj@shahmodi.com



Structure of FEMA

- Applies to the whole of India and all branches, offices and agencies outside India which are owned or controlled by a person resident in India.
- FEMA has 49 sections of which 9 (section 1 to 9) are substantive and the rest are procedural/ administrative
- Sec 37A – power to seize value equivalent Indian assets for overseas assets viz., foreign exchange, foreign security, immovable property *suspected to have been held* outside India held in contravention of Sec 4
- Section 46 of FEMA grants power to Central Government to make rules to carry out the provision of FEMA
- Section 47 of FEMA grants power to RBI to make regulations to implement its provisions and the rules made there under
- RBI is entrusted with the administration and implementation of FEMA



Structure of FEMA

- FEM ACT
- NOTIFICATIONS
- RULES
- MASTER DIRECTIONS
- A.P. DIR CIRCULARS
- FAQs

Substantive Provisions

Section	Description
1	Application and Commencement of FEMA
2	Definitions
3 to 9	Provisions relating to Regulations and Management of Foreign Exchange
10 to 12	Provisions relating to Authorized Person
13 to 15	Provisions relating to Contraventions and Penalties
16 to 38	Provisions relating to Adjudication, Appeal, Directorate of Enforcement and Power to Seize India assets
39 to 49	Miscellaneous Provisions



Notifications under FEMA

- RBI had initially issued 25 notifications, covering capital account transaction prescribed in Sec 6(3) & certain miscellaneous provisions
- 15 related to capital account transactions, 1 on Export of goods and services and 9 for other regulations
- Since original notifications have undergone many changes, RBI has started revising the notifications and till date has issued 15 revised notifications [3(R), 5(R), 6(R), 7(R), 9(R), 10(R), 11(R), 12(R), 13(R), 14(R), 15(R), 18(R), 21(R), 22(R) and 23(R)] carrying suffix (R) for easy identification along with the year in which they are published.
- https://www.rbi.org.in/Scripts/BS_viewfemanewnotification.aspx



Master Directions

- RBI has come up with Master Directions covering foreign exchange transactions.
- Master Directions consolidate instructions rules and regulations on the related subject.
- Master Directions are updated as and when there is change in rules/regulations or change in policy.
- Erstwhile Master Circulars thus have been withdrawn with issue of Master Directions.
- Till date, 19 Master Directions have been issued by RBI.
- https://www.rbi.org.in/scripts/FS_Notification.aspx?fn=5&fnn=2764



A.P. (Dir Series) Circulars

- Authorised Persons Directions issued by RBI u/s. 10(4) and 11(1) of FEMA to Authorized Persons (AP)
- These directions are called – **A.P. (Dir Series) Circulars**
- APs are Authorized Dealers, Money Changers and banks who are authorized to deal in Foreign Exchange
- These Circulars are operational instructions to AP by RBI
- Legal validity of these Circulars have been upheld in the case of Prof. Krishnaraj Goswami v. RBI, [2007 (6) Bom. CR 565]
- Court upheld the power of RBI to issue such Circulars based on powers conferred to RBI u/s. 10(4) & 11(1) & negated the contention that RBI has no jurisdiction to issue such Circulars



Preamble, Definitions and Importance of Forex for India

- Preamble- *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 foreign exchange market in India*
- Foreign Currency- *means any currency other than Indian currency*
- Foreign Exchange – *means foreign currency and includes, -*
 - *(i) deposits, credits and balances payable in any foreign currency*
 - *(ii) drafts, travellers cheques, letters of credits or bills of exchange, expressed or drawn in Indian currency but payable in foreign currency*
 - *(iii) drafts,.....or bills of exchange drawn by banks, institutions or Persons outside India, but payable in Indian currency*



Defn... Continued..

- Repatriate to India- *means bringing into India the realised foreign exchange and –*
- *(i) the selling of such foreign exchange to an authorised person in India in exchange for rupees, or*
- *(ii) the holding of realised amount in an account with an AP in India to the extent notified by the RB*
- *Transfer- includes sale purchase, exchange, mortgage, pledge, gift, loan or any other form of transfer or right title, possession or lien.*



Sec 8 of FEMA

- Realisation and Repatriation of Forex:
- *Save as otherwise provided in this Act, where any amount of forex is due or has accrued to any person resident in India, such person shall take all reasonable steps to realise and repatriate to India such forex within such period and such manner as may be prescribed by the RB*



CONCEPT OF RESIDENCE

Shah & Modi

CHARTERED ACCOUNTANTS



Residential Status under FEMA

- Under FEM Act residential status is of two types:
 - Person resident in India
 - Person resident outside India
- The Current Account Rules under FEMA, also refer to '**Person Resident but not permanently resident in India**'
- Under FERA, citizenship was considered as deciding factor
- FEMA lays emphasis on 'residing' which denotes permanency
- The definition of "Resident" is silent regarding the residential status of students going abroad for education.



Residential Status under FEMA

- **PERSON RESIDENT IN INDIA [Sec. 2(v)(i) of FEMA]:**

Residing in India for > 182 days during the course of preceding F.Y. but doesn't include

- going out of India or staying outside India

- for taking up employment
- for carrying business or vocation
- for any other purpose in such circumstances as would indicate his intention to stay outside India for uncertain period

- coming to India or staying in India otherwise than

- for taking up employment
- for carrying business or vocation
- for any other purpose in such circumstances as would indicate his intention to stay in India for uncertain period

- **PERSON RESIDENT OUTSIDE INDIA [Sec. 2(w) of FEMA]:** a person who is not resident in India.



Analysis of Definition

- Unlike Income tax, wherein residential status of a person is determined only on the basis of physical stay in India, under FEMA, it is the **intention** of 'leaving India' or 'coming to India' determines the residential status
- However, definition does refer to physical stay in India.
- The better view however should be – “**Intention**” prevails over “**Physical Stay**”.



Reference to FEMA Notification emphasizing “Intention”

- **Para 7 of Schedule 1 of FEMA Notification No. 5(R) – Deposit regulations**

NRE accounts should be re-designated as resident accounts or funds held may be transferred to RFC Accountsimmediately upon return to India for taking up employment or for carrying on business or for any other purpose indicating intention to stay in India.....

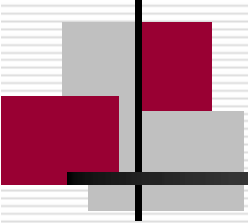
Above para does give an indication that physical stay is not the guiding factor.

- **Visit to India-** Same para states- where a/c holder is on a short visit to India the a/c may continue as NRE even during his stay in India.



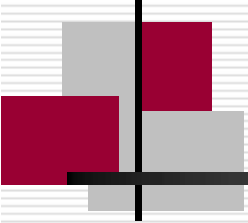
Physical Stay should be relevant only for acquisition of Immovable Property by Foreign Nationals other than OCI

- Press Release of Ministry of Finance dated 1st February 2009 – Government's advice on acquiring land by persons resident outside India
- In case of foreign nationals, physical condition to stay for more than 182 days is mandatory for buying of Immovable Property as Resident.
- Along with period of stay intention also needs to be established.
- Travel related documents and nature of Visa can establish intention of a person.



Residential Status under FEMA- Person Resident but not permanently resident

- Explanation to Schedule III of Current A/c Rules
-, 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 assignment, the duration of which does not **exceed 3 years**, is considered to be *a person resident but not permanently resident in India*.
- This is more in nature of facility available.
- Being resident but not permanently resident in India means a person is resident of India.
- Even his bank account is Resident account.



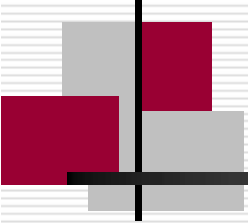
Residential Status under FEMA- Person Resident but not permanently resident

- A person resident but not permanently resident in India enjoys following facilities:
 - Such person can make remittance up to net salary (after deduction of taxes, contribution to provident fund and other deductions) – explanation to Schedule III of CAT Rules.
 - Reg 4 of Not 11(R)-[Possession & Retention of FC]-PRbNPRiI can possess FC without any limit- provided such FC was owned by him when he was NR and has been brought into India in accordance with FEMA.



Facilities of PRbNPRiI.. Contd...

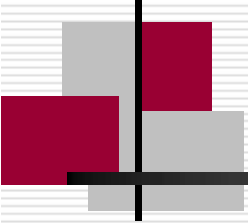
- An entity in India may remit PF or pension in respect of *expatriate staff* who are RbNPRiI (Reg 5 of 13R).
- *Expat-* means a person whose PF/pension fund is maintained outside India by his principal employer outside India [Explan to above Reg 5 of 13(R)]
- Such person who is not permanently resident may purchase a foreign security from out of his foreign currency resources outside India [Reg 4(c) of FEMA 120]
- Relaxed remittance facilities as stated above will apply to (i) citizen of foreign state other than Pakistan and (ii) even to Indian citizen who is on deputation to the office or branch or subsidiary or joint venture of foreign company- Para 3.2 of MD- Other Remittance Facilities



Residential Status under FEMA – Indian Students Studying Abroad

- A.P. (DIR Series) Circular No. 45 dated December 8, 2003
 - While taking up studies, students may have to take up job or seek scholarships to supplement their income. As a result their stay gets prolonged than what is intended while leaving India.
 - They are not dependent for a dominant part of their expenses on remittances from their households in India.

Hence, their stay will be for more than 182 days and intention will also be to stay outside India for uncertain period. Thus they **can be treated** as Non Resident Indians (NRI).



Accounts for Indian Students Studying Abroad

- Regulation 5(F)(6) of FEMA Notification No. 10R
 - Indian students studying abroad may open, hold and maintain foreign currency account with bank outside India during their stay outside India.
 - On return to India, after completion of studies, such an account will deemed to have been opened under the Liberalized Remittance Scheme



EMIGRATING INDIANS

Shah & Modi

CHARTERED ACCOUNTANTS



SECTION 6(5) of FEMA - STATUS OF ASSETS IN INDIA

- 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 such person when he was resident in India or inherited from a person who was resident in India.
- Assets (Share / Securities, Immovable Property and Indian Currency) which were acquired at time when a person was resident in India can be continued to be held even after he turns out non - resident.
- The same can even be transferred or invested.
- Further, NR can inherit the same from a resident u/s 6(5) of FEMA.



SECTION 6(5) of FEMA - STATUS OF OTHER ASSETS IN INDIA

- Whether other assets like Jewellery, Paintings, Silver Articles etc., interest in LLP or Partnership Firm can also be in terms of Section 6(5)?
- **Jewellery, Paintings, Silver Articles etc. -**
 - ❖ 6(5) only refers to specific assets viz. currency, securities and immovable property.
 - ❖ However intention is to permit NRI to own all assets which he was owning prior to turning NRI.
 - ❖ Thus, these assets can be continued.



SECTION 6(5) of FEMA - STATUS OF OTHER ASSETS IN INDIA

■ Interest in Indian LLP -

- ❖ Intention of 6(5) is to permit NRI to own all assets which he was owning prior to turning NRI.
- ❖ NRI can continue even as partner of Indian LLP even after becoming NRI.
- ❖ Fresh investment in LLP towards capital may be made through NRO to make it distinctively clear that fresh investment is also on non-repatriation basis.
- ❖ Fresh investment in form of loan cannot be made to LLP.
- ❖ Existing Loan to LLP may be continued. However repayment of loan by LLP or firm shall be made to NRO account.



SECTION 6(5) of FEMA - STATUS OF OTHER ASSETS IN INDIA

■ Interest in Indian Partnership Firm -

- ❖ Intention of 6(5) is to permit NRI to own all assets which he was owning prior to turning NRI.
- ❖ Unlike LLP, NRI can even continue to be as partner of Indian Partnership Firm even after becoming NRI.
- ❖ Fresh investment as capital in firm to be made compulsorily through NRO.
- ❖ Fresh Loan cannot be given.
- ❖ Indian Partnership Act permits firm having all NRIs/OCIs partners. No need of having resident partner.



Impact on transactions done at time when person was resident in India

Bank Accounts:

- Existing resident account should be re-designated to NRO account if person leaves India for uncertain period (for employment or business or vocation outside India).
- Balances in EEFC and RFC(D) can be credited to NRE/FCNR(B) accounts

Demat Accounts:

- Sec 6(5) permits NRI to continue to own securities which were acquired while person was resident of India.
- Securities in Demat account can be continued to be held by NRI.
- NRI needs to Intimate Depository about change in his residential status.



Impact on transactions done at time when person was resident in India

Demat Accounts:

- Schedule 3 and 4 of Non Debt Instrument Rules permits NRI to make portfolio on repatriation and non-repatriation basis.
- The investment in securities (Demat Account) existing on date of becoming NRI will be characterized as non-repatriable investment.

Insurance Policies:

- Life /General Insurance Policy taken in India can be continued.
- No permission required for payment of premium.



Impact on transactions done at time when person was resident in India

PPF Account:

- As per F.No. 01/10/2016-NS dated 23rd February, 2018 an NRI can continue to operate PPF account and continue to invest further till the time it matures (after 15/5 years)
- After maturity account cannot be renewed.

Foreign Currency Investment made outside India under LRS and ODI:

- All foreign currency investment made under LRS can be continued.
- In case of ODI transactions, upon turning NRI it will no longer remain ODI. Intimation to RBI is required to be given and Form ODI Part III will be required to be filed for cancellation of UIN. ²⁹



Impact on transactions done at time when person was resident in India

Investment in Immovable Property outside India:

- Property bought jointly by Father and Son in 2018 under LRS.
 - ❖ Son intends to go for studies abroad in 2020.
 - ❖ Son intends to go for employment in 2020.
- Implications of Gift of property by Son to father?



Gift of Overseas Property NRI/OCI to Resident

- ❖ Gift of immovable property situated outside India from NRI/OCI to resident is under approval route.
- ❖ Ref – FEMA Notification No. 7(R).
- ❖ Inheritance to Resident Indian is however under Automatic Route.



Advantages of becoming NRI/OCI

- The income earned abroad need not be repatriated to India. He can make investments out of these earnings. He can retain foreign assets / security even after his return to India.
- NRI can remit up to USD 1 million out of sale proceeds/balances in their account maintained with an AD in India
- NRI can open a NRE / NRO Account.



Caution Points upon becoming NRI

- ✓ The NRI may continue to subscribe to the PPF till maturity. However, they are not eligible to renew/ continue the PPF Account after maturity period of 15 years.
- ✓ The NRI cannot invest in agricultural land and plantations. They may continue to own existing Agricultural land acquired before attaining NRI status.
- ✓ The NRI cannot continue to be a partner in a partnership firm which is involved in agricultural/plantation activity or real estate business, i.e. dealing in land and immovable property
- ✓ Taking Life Insurance Policy of Indian Insurer while staying overseas can be cumbersome process and many private life insurance companies want presence of Insured in India.
- ✓ NRI cannot receive loan in INR from non-relative in India.



RETURNING INDIANS

Shah & Modi

CHARTERED ACCOUNTANTS



SECTION 6(4) of FEMA - STATUS OF ASSETS OUTSIDE INDIA

- 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.
- Assets (Share / Securities, Immovable Property and Foreign Currency) which were acquired at time when a person was resident outside India can be continued to be held even after he turns resident.
- The same can even be transferred or invested.
- Further, R can inherit the same from a non resident u/s 6(4) of FEMA.



SECTION 6(4) of FEMA - COVERS FOLLOWING TRANSACTIONS

- **Foreign currency accounts** opened and maintained by such a person outside India when he was resident outside India;
- **Income earned through employment or business or vocation outside India** taken up or commenced while 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;
- **Foreign exchange including any income** arising there from, 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.



SECTION 6(4) of FEMA - COVERS FOLLOWING TRANSACTIONS

- 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 therefore are met exclusively out of funds forming part of eligible assets held by them and the transaction is not in contravention to extant FEMA provisions.



SECTION 6(5) of FEMA - STATUS OF OTHER ASSETS OUTSIDE INDIA

- Whether other Movable Assets like Jewellery, Paintings, Silver Articles etc., or Other Assets like interest in LLP or Partnership Firm outside India can also be continued in terms of Section 6(4)?
 - ❖ 6(4) also only refers to specific assets viz. currency, securities and immovable property.
 - ❖ However intention seems to be to permit resident to own all assets outside which he was owning prior to turning resident.
 - ❖ Thus, these assets can be continued.
 - ❖ However with regards to Interest in Firm with unlimited liability, it would be advisable to take RBI permission.
 - ❖ What about Crypto Currency?



Impact on transactions done at time when person was resident outside India

ODI-FDI structure:

- An individual was having a company outside India while he was being a non-resident.
- At that time such overseas company had made FDI in India.
- Upon return to India 6(4) permits to continue existing investment outside India.
- Therefore, whether ODI-FDI structure still be continued to be allowed?
- Whether Overseas company [i.e. 6(4) - Company] can make fresh FDI in India? Will it amount to round tripping?



Impact on transactions done at time when person was resident outside India

Bank Accounts:

- Foreign Bank Accounts can be continued to be held u/s 6(4).
- NRE accounts should be re-designated to resident accounts immediately upon return to India (for employment or business or vocation outside India).
- Funds in NRE accounts can even be transferred to RFC at option of the account holder.
- NRO accounts to be re-designated to resident rupee accounts.
- FCNR deposits can be continued till maturity. On maturity the same shall be converted to rupee deposit accounts or RFC account.



Impact on transactions done at time when person was resident in India

Insurance Policies:

- Life /General Insurance Policy taken outside India can be continued.
- No permission required for payment of premium.
- Maturity proceeds or amount of any claim due shall be repatriated to India within 7 days of receipt.



Resident Foreign Currency (RFC) Account

- Individuals can open RFC Account
- No restrictions on utilization of funds in / outside India including restrictions of Schedule III to Current Account Rules.
- However Schedule I and II restrictions will apply like purchase of overseas lottery etc.
- Permissible Credits:
 - received as pension or any other superannuation or other monetary benefits from his employer outside India; or
 - realised on conversion of the assets referred to in sub-section (4) of section 6 of the Act, and repatriated to India; or
 - received or acquired as gift or inheritance from a person referred to in sub-section (4) of section 6 of the Act; or
 - referred to in clause (c) of section 9 of the Act, or acquired as gift or inheritance there from; or



Resident Foreign Currency (RFC) Account

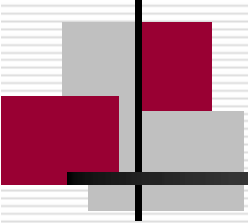
- received as the proceeds of life insurance policy claims/ maturity/ surrender values settled in foreign currency from an insurance company in India permitted to undertake life insurance business by the Insurance Regulatory and Development Authority.
- Balances in NRE.FCNR account on change in residential status.



CAPITAL AND CURRENT ACCOUNT TRANSACTIONS

Shah & Modi

CHARTERED ACCOUNTANTS



Introduction - Concept of Capital & Current account transaction

- Concept of Cap A/c & Cur A/c was absent in FERA
- The drawal of foreign exchange was regulated without differentiating between Cap or Cur A/c
- It was absent even after introduction of New Industrial Policy of 1992
- It was introduced in FEMA, 1999 which replaced FERA, 1973
- Capital and current a/c are Economic concept and not an Accounting concept



FEMA Structure dealing with Capital Account Transaction

Section 6(1) - Capital Account Transaction - Subject to the provisions of sub-section (2), any person *may sell or draw* foreign exchange *to or from an authorised person* for a capital account transaction.

The amendments to Section 6 which were proposed in Finance Act 2015, have been notified with effect from 15th October 2019.

- Section 6(2)(a) - The RBI may, in consultation with the Central Government specify any class or classes of capital account transactions, **involving debt instruments**, which are permissible, the limit up to which foreign exchange shall be admissible for such transactions, and any conditions which may be placed.
- Accordingly, Foreign Exchange Management (Debt Instrument) regulations 2019 notified on 17th October 2019.



FEMA Structure dealing with Capital Account Transaction

- Section 6(2A) - CG may, in consultation with the RBI specify any class or classes of capital account transactions, **not involving debt instruments**, which are permissible, the limit up to which FE shall be admissible for such transactions, and any conditions which may be placed.
- Accordingly, CG issued Foreign Exchange Management (Non-Debt Instruments) Rules 2019 - 17th October 2019



Capital Account Transaction

- Once notified, all Capital Account transactions, except involving debt instruments will be regulated by the CG, which are currently being regulated by the RBI.
- From Section 6(1) it is clear that a person can only sell or draw foreign exchange from an authorised person for capital account transactions. Dealing in foreign exchange other than through Authorized Person is not permitted.
- Section 3(a) also prohibits- dealing in or transferring of any foreign exchange to any person other than by authorised person.



Definition - Capital Account Transaction

Section 2(e) -

Capital Account transaction means *a transaction –*

➤ *which alters assets or liabilities including contingent liabilities, outside India of person resident in India or*

➤ *assets and liabilities in India of persons resident outside India and*

➤ *includes transactions referred to in sub-section (3) of Section 6.*



Capital Account Transaction

Section 6(3) – Lists the Capital Account Transactions that are prohibited, restricted or regulated by RBI (capital account transactions as also referred to in definition of Capital Account Transaction in Section 2(e)]

- a) Transfer or issue of any security by a person resident in India
- b) Transfer or issue of any security by a person resident outside India.
- c) Transfer or issue of any security or foreign security by any branch, office or agency in India to a person resident outside India.
- d) Any borrowing or lending in foreign exchange in whatever form or by whatever name called



Capital Account Transaction

- e) Any borrowing or lending in Indian rupees in whatever form or by whatever name called between person resident in India and a person resident outside India.
- f) Deposits between persons resident in India and persons resident outside India
- g) Export, import or holding of currency or currency notes.
- h) Transfer of immovable property outside India, other than a lease not exceeding five years, by a person resident outside India
- i) Acquisition or transfer of immovable property in India, other than a lease not exceeding five years, by a person resident outside India.



Capital Account Transaction

- j) Giving of a guarantee or surety in respect of any debt, obligation or other liability incurred –
- By a person resident in India and owed to a person resident outside India; or
 - By a person resident outside India.

Apart from above transactions, RBI has made FEM (Capital Account Transactions) Regulations, 2000. Schedules I and II of this regulation specify the classes of capital account transactions of resident and non-residents for which foreign exchange may drawn or sold to an authorised person.

Capital Account Transaction

Sr. No.	Transactions	Corresponding Notification	Corresponding Section of FEMA
1	Permissible Capital Account Transactions	No. 1	Sec 6(2) read with Sec 47 (2)
2	Transfer or issue of any security or foreign security by any branch, office or agency in India of a person resident outside India	No. 2	Sec 6(3)(c) read with Sec 47(2)
3	Any borrowing or lending in foreign exchange in whatever form or by whatever name called	No. 3(R) dated 17.12.2018	Sec 6(3)(d) read with Sec 47(2)
4	Deposits between persons resident in India and persons resident outside India	No. 5(R) dated 01.04.2016	6(3)(f) read with Sec 47(2)

Capital Account Transaction

Sr. No.	Transactions	Corresponding Notification	Corresponding Section of FEMA
5	Export, import or holding of currency or currency notes	No. 6(R) dated 29.12.2015	Sec 6(3)(g) read with Sec 47(2)
6	Transfer of immovable property outside India, other than a lease not exceeding five years, by a person resident in India	No. 7(R) dated 21.01.2016	Sec 6(3)(h) read with Sec 47(2)
7	Giving of a guarantee or surety in respect of any debt, obligation or other liability incurred - (i) by a person resident in India and owed to a person resident outside India (ii) by a person resident outside India	No. 8	Sec 6(3)(j) read with Sec 47(2)
8	Insurance	No. 12(R) dated 29.12.2015	Sec 47(2)



Capital Account Transaction

Sr. No.	Transactions	Corresponding Notification	Corresponding Section
9	Remittance of Assets	No. 13 (R) dated 01.04.2016	Sec 47
10	Transfer or issue of any Foreign Security	No. 120 dated 07.04.2004	Sec 6(3)(a) read with Sec 47
11	Acquisition or transfer of immovable property in India, other than a lease not exceeding five years, by a person resident outside India	No. 21 (R) dated 26.03.2018	Sec 6(3)(i) read with Sec 47(2)
12	Establishment in India of Branch or Office or other place of business	No. 22 (R) dated 31.03.2016	Sec 6(6)



Dues payable on use of credit cards- whether in the nature of borrowing

- Explanation to Reg 3 of Notification No.3(R)
- - *use of CC (a) in India by a PROI or (b) outside India by a PRII shall not be deemed as borrowing or lending in INR/foreign exchange*



Cap A/c Transaction and Contingent liability of NR

Guarantee by Person Resident Outside India:

- The definition of Cap A/c Transaction does not include contingent liability of a person resident outside India. However, Sec 6(3)(j) & Schedule II (c) to Notification 1 includes in the list of capital account transaction guarantee given by a person resident outside India to any person resident in India.
- There is no reporting as such for guarantee given by non-resident in respect of borrowing in rupees by resident Indian where lender is also another resident Indian.
- In case of invocation of guarantee where liability is paid by non-resident, the principal debtor (i.e. Indian borrower) can make payment to such non-resident guarantor under general permission.



Guarantee by NR contd...

- Master Direction on ECB, TC & Structured Obligations dt 26.03.2019:
- Para 19- Domestic rupee borrowing between two Residents based on guarantee of NR doesn't have any FEMA implications until the guarantee is invoked.
- Upon invocation of Guarantee & payment by NR, such NR can enforce recovery and also repatriate such sum, if remitted from abroad or paid out of NRE/FCNR a/c.- General Permission

Gift Transactions

- Gift of sum of money by resident to a non-resident or non-resident to resident is a Current A/c Transaction.
- Gift of foreign security is a Capital A/c Transaction having following implications:

Donor	Donee	Remarks
NR	R	Permissible Reg 22(1)(i) of 120
R	R	Not covered by general permission
R	NR	Not covered by general permission

- Inheritance of foreign security:

Donor	Donee	Remarks
NR	R	Permissible Reg 22(1)(iii) of 120
R	R	Permissible Reg 22(1)(iii) of 120
R	NR	Not covered by general permission



Gift Transactions

- Gift and inheritance of Immovable Property Situated outside India:

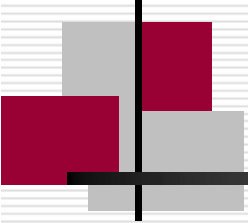
Donor	Donee	Remarks
NR	R	Not covered by general permission
R	R	Regulation 5(1)(a) for Sec 6(4) cases and 5(2) of Not. 7(R)
R	NR	Not covered by general permission

- In terms of Section 4 of FEMA, 1999 – foreign exchange, foreign security or any overseas immovable property must be held as per permissible modes of FEMA.
- Contravention of this can lead to penal consequences under Section 13(1A) – Penalty up to three times and seizure of equivalent assets in India.



Settling Property in Trust

- Resident becoming beneficiary in an overseas trust – As such there is no reporting.
- However, income earned by resident beneficiary needs to be repatriated within 180 days (Reg 7 of Notification No. 9R)
- Resident settling properties in a trust having NRI beneficiaries.
 - The assets settled should be FEMA compliant and trustees should be resident Indian as per FEMA.
 - **FEMA Master Direction No. 13 – Remittance of Assets- Para 3.2(iii)** - *in case settlement is done without retaining any life interest in the property i.e. during the lifetime of the owner/parent, it would tantamount to regular transfer by way of gift and the remittance of sale proceeds of such property would be guided by the extant instructions on remittance of balance in the NRO account;*



Change in nature of Transaction due to passage of time- current a/c transaction turning capital a/c

As per Master Direction on Import of Goods and Services:

- Import dues should be paid within six months from the date of shipment. If not paid extension must be obtained.
 - Deferred Payment Arrangements (suppliers and buyers credit) up to five years, are treated as Trade Credit and guidelines relating to same must be followed.
-
- Trade Payables more than six months and up to three years are allowed by RBI.
 - Extension needs to be obtained for Trade Payable outstanding for more than six months.
 - Trade Payable outstanding more than 3 years are treated as Deemed ECB.



Reference to RBI Compounding Orders

Delayed payment of import dues/fees for more than six months were treated as ECB.

➤ **Outstanding Fees:**

- TWI India Pvt. Ltd - CA Order No. 3945/2016 dated-31.08.2016
- Contravention relates to delayed payment of outstanding fees by subsidiary company in India to its parent in UK.
- Parent rendered services such as training, support, certification etc., every year and charged to its subsidiaries.
- The invoices remained outstanding for more than 180 days and were treated as “Trade Payable” in books of subsidiary.
- RBI granted post facto approval for remittance and also compounded contravention under Reg 5(3) of erstwhile FEMA Notification No. 3.



Reference to RBI Compounding Orders

Delayed payment of import dues/fees for more than six months were treated as ECB.

- **Outstanding dues against import of goods:**
 - **AMC Diamonds - CA Order No. 3934/2016 - dated 13.07.2016**
 - Indian company imported goods on credit from various exporters.
 - There was delay in making payment beyond six months.
 - RBI allowed to make payment and granted post facto approval.
 - RBI compounded contravention under Reg 5(3) of erstwhile FEMA Notification No. 3

- **Intercat Equipment - CA Order No. 3861/2015 - dated 02.06.2016**



Whether following transactions are in nature of Capital Account Transaction?

- Factoring of Export Invoices
 - Say, at Interest rate of 5%
 - Factoring Commission of 1.8%
 - Delayed Payment Interest @ 4%
- Effect of terms & conditions - if factoring is -
 - “With recourse” basis, or
 - “Non-recourse” basis
- Refer AP (Dir Series) Circular No.5 of July 16, 2015 on permitting factoring on ‘Non Recourse’ basis.



Definition - Current Account Transaction

Section 2(j) -

Current Account transaction is transaction other than a capital account transaction and generally includes:

- i. Payments due in connection with foreign trade, Short term banking and credit facilities.
- ii. Payment due as interest on loan and income from investment.
- iii. Remittances for living expenses of parent, spouse and children residing abroad.
- iv. Expenses in connection with foreign travel, education and medical care of parents, spouse and children.



Current Account Transaction

- Current account transaction is a transaction other than a capital account transaction
- Current account transactions are governed by Foreign Exchange Management (Current Account Transaction) Rules, 2000 ("Current Account Transactions Rules").
- India is signatory to WTO Agreement and in terms of Article VIII; it states that “.....no member shall, without the approval of the Fund (IMF), impose restrictions on the making of payments and transfers for current international transaction.”



Current Account Transaction

- Current account transactions are divided into 3 schedules in Current Account Transactions Rules:-
 - Schedule I – Prohibited Transactions
 - Schedule II – Transactions requiring prior approval of Government of India
 - Schedule III – Transactions requiring prior approval of RBI
- Drawal of foreign exchange is prohibited for –
 - Transactions specified in Schedule I; or
 - Travel to Nepal and / or Bhutan; or
 - Transaction with person resident in Nepal or Bhutan (this prohibition may be relaxed by special approval).



Restrictions on use of RFC funds for Current Account Transactions?

Current Account Rules:

- No restrictions on utilization of funds held in RFC account in /outside India including restrictions of Schedule II and Schedule III to Current Account Rules (Refer provisos to Rule 4 and 5 of CAT Rules).
- Schedule I does not have such relaxation and therefore it seem restrictions will apply for funds held in RFC account for purchase of overseas lottery, football pools, sweepstakes etc.

Is there a contradiction to above upon reading Reg 4(B)(2) of FEMA Notification No. 10R

- Reg 4(B)(2) of Notification No. 10R mentions that funds in RFC account shall be free from any restrictions regarding utilisation of foreign currency balances including any restriction on investment in any form, by whatever name called, outside India.



Current Account Transaction

Schedule I (Rule 3): Transactions which are prohibited

- Remittance out of lottery winnings (*)
- Remittance of income from racing/riding etc., or any other hobby
- Remittance for purchase of lottery tickets, banned/prescribed magazines, football pools, sweepstakes etc.
- Payment of commission on exports made towards equity investment in JV/WOS abroad of Indian companies.
- Payment of commission on exports under Rupee State Credit route except commission up to 10% of invoice value of exports of tea and tobacco.
- Payment related to 'Call Back Services' of telephones
- Remittance of interest income of funds held in Non-resident Special Rupee Scheme A/c.

(NOT PERMISSIBLE EVEN FROM RFC and EEFC ACCOUNT)

- * - In terms of FDI Policy even technology collaboration (franchise, trademark, brand name, management contract is prohibited for lottery business and gambling and betting)



Current Account Transaction

Schedule II (Rule 4) Transactions requiring prior approval of Government:

Purpose of remittance	Ministry/Department of Govt. of India
▪ Cultural tours	Ministry of Human resources Development
▪ Advertisement in foreign print media for purpose other than promotion of tourism, foreign investments and international bidding (exceeding USD 10,000) by a State Government and its Public sector undertaking	Ministry of Finance
▪ Remittance of freight of vessel chartered by a PSU	Ministry of Surface Transport
▪ Payment of import [through ocean transport] by a Govt. department or a PSU on CIF basis	Ministry of Surface Transport

Current Account Transaction

Purpose of remittance	Ministry/Department of Govt. of India
<ul style="list-style-type: none"> Multimodal transport operators making remittance to their agents abroad 	Registration Certificate from the Director General of Shipping
<ul style="list-style-type: none"> Remittance of hiring charges of transporters by TV channels, internet service providers 	Ministry of Information and Broadcasting, Ministry of Communication and Information technology
<ul style="list-style-type: none"> Remittance of container detention charges exceeding rate prescribed by Director General of Shipping 	Ministry of Surface Transport
<ul style="list-style-type: none"> 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 USD 1,00,000 	Ministry of Human Resources Development (Department of Youth Affairs and Sports)
<ul style="list-style-type: none"> Remittance for membership of P&I club (Association of Marine Insurance provider) 	Ministry of Finance



Current Account Transaction

Schedule III (Rule 5): Prior Approval of RBI

Facilities for Individuals - Individuals can make remittance within limit of USD 2,50,000 for following facilities. However, any additional remittance in excess of said limit shall require RBI approval.

- 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 specialised 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.



Current Account Transaction

- For items mentioned at (iv), (vii) and (viii), individual may remit amount in excess of USD 2,50,000 if it is so required by a country of emigration, medical institute offering treatment or the university.



Current Account Transaction

Facilities for persons other than individuals – Following remittances by persons other than individuals shall require prior approval of RBI

- Donations exceeding 1% of their foreign exchange earnings during the three financial years or USD 5,00,000 whichever is less.
- Commission per transaction to agents abroad for sale of residential flats or commercial plots in India exceeding USD 25,000 or 5% of inward remittance whichever is more.



Current Account Transaction

- Remittances exceeding USD 10 million **per project** for any consultancy services in respect of infrastructure projects and USD 1 million **per project** for other consultancy services procured from outside India.
 - Whether the above referred limits of USD 1 and 10 million are qua project or qua foreign consultant?
 - Compounding Order No. 3950/2016 dated 09.09.2016 in case of Jaguar Buildcon Pvt. Ltd. – remittance exceeding USD 1 million to various consultants for single project a contravention.



Current Account Transaction

- **'Infrastructure Sector'** has the same meaning as given in the Harmonised Master List of Infrastructure sub-sectors approved by Government of India vide Notification F. No. 13/06/2009-INF as amended vide Notification dated 14th November 2017.

Thus infrastructure sector and sub-sectors for the purpose of ECB include (Para 1(iv)(A)(a) of Schedule I of FEMA 3):

- Transport and Logistics
- Energy
- Water and Sanitation
- Communication
- Social and commercial infrastructure (includes Educational Institutions/Sports Infrastructure/Hospitals/Tourism Infrastructure/Common Infrastructure for Industrial Parks and other parks with industrial activity/Post harvest storage infrastructure/terminal Markets/Soil Testing Laboratories/Cold Chain/Affordable Housing)



Current Account Transaction : Pre-incorporation Exps

- Remittances exceeding 5% of investment brought into India or USD 1,00,000 whichever is higher for reimbursement of pre-incorporation expenses by entity in India.



Current Account Transaction - Unincorporated Joint Ventures

- Unincorporated Joint Ventures - Co-operation Agreements/Strategic Alliances
- It's a contractual relationship/arrangement like a cooperation agreement or a strategic alliance wherein the parties agree to collaborate as independent contractors rather than shareholders in a company or partners in a legal partnership.
- Co-operation agreements / strategic alliances can be employed for the following types of business activities:
 - Technology transfer agreements
 - Joint product development
 - Purchasing agreements
 - Distribution agreements
 - Marketing and promotional collaboration



Current Account Transaction - Unincorporated Joint Ventures (UJV)

Account in India by Unincorporated Joint Ventures - Regulation 7 of FEMA Notification 5(R):

- UJV of foreign companies / entities along with Indian entities for executing a contract in India, may be allowed to open non interest bearing foreign currency account and a SNRR account.
- AD Bank may allow the same subject to directions of RBI.
- These accounts shall be to undertake transaction in ordinary course of business by UJV and Indian entity.
- Debits and Credits to account shall be incidental to business requirement of UJV.
- Tenure of account shall be concurrent to tenure of contract / period of operation of UJV.
- Opening of accounts by companies / entities of Pakistan / Bangladesh ownership / nationality would require prior approval of RBI.



Current Account Transaction

- Royalties and Lump Sum Fees

- Earlier there were monetary caps on remittances (both lumpsum fees and royalties) made for technology collaborations and license or use of trademark / brand name.
- Now there are no restrictions and the payments towards the lumpsum fees or royalties for technology collaborations and license or use of trademark / brand name can be made under the automatic route, without any monetary cap
- Refer Para 4.9 of MD- Other remittance facilities

The limits were there in Schedule II which read as under:

Remittances under technical collaboration agreements where payments of royalty exceeds 5% on local sales and 8% on exports and lump sum payments exceeds USD 2 million.

This has been removed w.e.f. 16/12/2009



Current Account Transaction

- Advance against exports of goods can be received by an exporter *from a buyer or third party named in export declaration.*
- Interest can be paid on advance payment (rate of interest shall not exceed LIBOR plus 100 basis points).
- Shipment of goods needs to be made within one year from the date of receipt of Advance.
- In case of advance against export of services, there is no specific inward remittance purpose code and hence poses practical difficulties.



Current Account Transaction

- Whether Deposit given by NRI for acquiring immovable property on rental is a Capital Account Transaction?
- Whether Deposit given by an Indian Resident towards Import of Machinery to non-resident for Trade fair Exhibition is a Capital Account Transaction?

Reference can be drawn from A.P. DIR 59 dated April 13, 2016 wherein it is mentioned that *“keeping deposits with an Indian company by persons resident outside India, in accordance with section 160 of the Companies Act, 2013, is a current account (payment) transaction and, as such, does not require any approval from Reserve Bank. All refunds of such deposits, arising in the event of selection of the person as director or getting more than twenty five percent votes, shall be treated similarly”*.



Conversion of Current Account Transaction to Capital Account Transaction

- Para 1(d) of Schedule 1 of FEMA **Non Debt Instrument Rules 2019 (NDI Rules)** Issue of Shares against Import of capital goods/machinery/equipment or pre-incorporation expenses.
- Para 1(e) of Schedule 1 of FEMA NDI Rules, 2019 - Shares can be issued against **any funds payable**, remittance of which does not require prior approval of RBI or government.

Examples of **any other funds payable** - payments for use or acquisition of intellectual property rights, for import of goods, payment of dividends, interest payments, consultancy fees, etc. - Refer A.P. DIR 52 dated February 11, 2016



Change in nature of Capital Account Transaction

- Conversion of ECB to Equity Shares:
 - The activity of borrowing company should be under automatic route or approval as required must be obtained.
 - It must comply with FDI guidelines.
- In case of Overseas Direct Investment, conversion of loan to equity is under automatic route whereas for conversion of equity to loan prior approval is required.

Questions ...





THANK YOU

FIRST DESERVE

AND

THEN DESIRE!!

