

FEMA – AN OVERVIEW

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FEMA – AN OVERVIEW

BASIS OF EXCHANGE CONTROL LAW

- An economic legislation
- Legal regulation on scarce resource of ‘foreign exchange’
- Cannot be a static law – but dynamic – Central Government retains power to suspend or relax the law
- How much foreign exchange is sufficient for a country?
- Gulf war of 1990 foreign exchange crisis – a trigger factor
For liberalization in the law, followed by Industrial Policy of 1991

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“CONTROL” TO “MANAGEMENT”

- Change in forex balance – 1991 \$ 500 million to 34 billion in 1999
- Today it has crossed \$ 470 + billion & growing!
- Major component is software exports – major concern is crude oil import. The coming decade is going to change this (e.g. EVs & Solar).
- This necessitated shift in focus – from ‘permission’ to ‘promotion’
- ‘Control’ became allergic and the shift was ‘management’
- From Quasi-criminal old FERA to Civil new law FEMA

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SALIENT FEATURES OF FEMA

- Focus of law changed – from accounting & controlling in FERA to orderly development of forex market and, facilitating external payments
- Alignment of certain definitions such as Person, Person Resident in India, similar to Income Tax law
- Transaction regulated according to Nature – Current A/c and Capital A/c Transactions

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SALIENT FEATURES OF FEMA

- **Rigour of penal provisions diluted**
 - quantum of penalty reduced
 - concept of Mens rea abolished
 - No automatic imprisonment. Arrest only if penalty is not paid
 - Penalty subject to Adjudication
 - Compounding made possible
- **Central Government retains residuary power to suspend / relax the law**

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CAPITAL ACCOUNT TRANSACTION U/S 2(e)

- What is Capital A/c for Accounting – Assets (A) or Liabilities, including Contingent liabilities (L) OR simply a Balance Sheet Item, as compared with P&L A/c item.
- Legally there shall be 'alteration' – that is, purchase or sale, addition or deletion.

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CAPITAL ACCOUNT TRANSACTION U/S 2(e)

- This can be understood in a logical way: Location of person and A&L
- If the A&L and the person doing the Transaction are located cross-border, then it is a Capital A/c Transaction under FEMA. Otherwise not. E.g. FDI, ODI, Guarantees, ECB, FII, immovable properties in India are all Capital A/c Transactions.

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CAPITAL ACCOUNT TRANSACTION U/S 2(e)

- Capital A/c Transactions include items specified u/s 6(3) as well.
- Capital A/c Transactions continued to be regulated.

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Permissible Capital Account Transactions:-

The FEM (Permissible Capital Account Transactions) Regulations permit various Capital A/c Transactions of Person Resident in India or “residents”.

- FDI or Investment in foreign securities or Overseas Direct Investment (ODI)
- Loans raised in foreign security or External Commercial Borrowings (ECB)
- Transfer of immovable property outside India
- Remittance of Capital asset outside India
- Loans by residents to non-residents & vice-versa

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CURRENT A/C TRANSACTION[S. 5]

- Definition u/s 2 (j) is by exclusion. Current A/c Transaction is what is not a Capital A/c Transaction. It expressly includes the following:-
- Payments due in connection with foreign trade, other current business, services, and short-term banking and credit facilities in the ordinary course of business

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CURRENT A/C TRANSACTION

- Payments due as interest on loans and as net income from investments
- Remittances for living expenses of parents, spouse and children residing abroad AND
- Expenses in connection with foreign travel, education and medical care of parents, spouse and children.
- Current A/c transactions are free from Regulation– barring a limited prohibition / regulation as per the FEM [Current A/c Transactions] Rules 2000 [S.5 proviso]– regardless of ceiling limits, monetary or percent age wise.

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PENALTY PROVISIONS

- Not without adjudication
- Quantum [S. 13(1)]: Thrice where quantifiable. Where not quantifiable max. Rs. 2 lakhs.(when not quantifiable and if a continuing offence- 5000/- for every day after the first day the contra continues)
- [S 7]--Order of Adjudicating officer could be appealed to SD or Tribunal
- [S. 14(1)]--Arrest, only if penalty is not paid within 90 days or appealed against
- [S.15]--From February 1st 2005 most of the contraventions are compoundable
- LSF provided to make compliance business-friendly

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CENTRAL GOVERNMENT POWER

- The Central Government retains power to suspend / relax based on National Interests

SUMMING UP:-

Dissect any proposed Transaction as to its Nature: - Current A/c or Capital A/c.

- If current A/c, one can do it through banking system itself.
- If Capital A/c, it is still regulated. One has to comply with procedures, as to ceilings, forms, approval, and other procedures. Most of the Capital A/c Transactions are also progressively getting liberalised.