Certificate Examination in

Foreign Exchange Operations

(2020-2021)
(IIBF & Other Exams)

Read FEDAI 7 Books prescribed by IIBF

Srinivas Kante

Compiled by

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About Certificate Examination in Foreign Exchange Operations

EXAMINATION OBJECTIVE:
The objective of the course is to make the bank officials familiar with Foreign Exchange operations. This exam is being introduced pursuant to the recommendation of a committee of RBI.
ELIGIBILITY: Open for employees working with Authorised Dealer (AD) Member Banks of FEDAI.
SUBJECT OF EXAMINATION: Foreign Exchange Operations
PASSING CRITERIA: Minimum marks for pass in the subject is 50 out of 100
EXAMINATION FEES: Rs.1000/- *
** Plus Convenience charges and Taxes as applicable.*
Please Note : Candidates are required to Register for every attempt separately.
As a measure to streamline the traffic for registration, Institute will charge regular examination fee to candidates who registers for the examination during the regular open period of registration. **For the extended days of registration, late fee of** Rs.**200 plus taxes, will be charged in addition to regular examination fee.** This extended days of registration, also gives candidates addition opportunity to register for the examination, having missed the regular open period of registration.
The fee once paid will **NOT** be refunded or adjusted on any account.
MEDIUM OF EXAMINATION:
Examination will be conducted in English only.
PATTERN OF EXAMINATION:
(i) Question Paper will contain 100 objective type multiple choice questions for 100 marks.

(ii) The examination will be held in Online Mode only.

(iii) There will NOT be negative marking for wrong answers.

DURATION OF EXAMINATION:
The duration of the examination will be of 2 hours.
PERIODICITY AND EXAMINATION CENTRES:
a) Examination will be conducted on pre-announced dates published on IIBF Web

Site. Institute conducts examination on half yearly basis, however periodicity of the examination may be changed depending upon the requirement of banking industry.
b) List of Examination centers will be available on the website. (Institute will conduct examination in those centers where there are 20 or more candidates.)

PROCEDURE FOR APPLYING FOR EXAMINATION
Application for examination should be registered online from the Institute's website www.iibf.org.in. The schedule of examination and dates for registration will be published on IIBF website

STUDY MATERIAL / COURSEWARE
Candidates to contact FEDAI (Foreign Exchange Dealer's Association of India) office through their bank branch / office and place order for study material. The same will be sent to the respective bank branch / office. Candidates can also buy the same by visiting personally to the office of FEDAI office on production of ID card.
Candidates should not deposit Cash directly in the account of FEDI under any circumstances.
FEDAI STUDY MATERIAL
(For Members Banks only)

Sr. No.	**Title of Book(s)**
1.	FEDAI Role & Rules, Foreign Exchange Rates & Risk Management
2.	Regulatory Requirements under FEMA-1999 (Vol-I)
3.	Regulatory Requirements under FEMA-1999 (Vol-II)
4.	Documentary Credits & Standby Credits
5.	Export Finance
6.	Foreign Trade Policy 2015-2020
7.	Booklet on Forex Facilities for Resident & Non-Resident Indians

Name
Bank Name & Address
Tel No. / Cell No.
Details of Payment
(UTR No. / Cheque No.)
All correspondence for this purpose may be done with e-mail ID: book@fedai.org.in
Candidates are advised to make full use of the courseware. However, as banking and finance fields are dynamic, rules and regulations witness rapid changes. Therefore, the courseware should not be considered as the only source of information while preparing for the examinations. Candidates are advised to go through the updates put on the IIBF website from time to time and go through Master Circulars / Master Directions issued by RBI and publications of IIBF like IIBF Vision, Bank Quest, etc. All these

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sources are important from the examination point of view. Candidates are also to visit the websites of organizations like RBI, SEBI, BIS, IRDAI, FEDAI etc. besides going through other books & publications covering the subject / exam concerned etc. Questions based on current developments relating to the subject / exam may also be asked.

Cut-off Date of Guidelines / Important Developments for Examinations

The Institute has a practice of asking questions in each exam about the recent developments / guidelines issued by the regulator(s) in order to test if the candidates keep themselves abreast of the current developments. However, there could be changes in the developments / guidelines from the date the question papers are prepared and the dates of the actual examinations.

In order to address these issues effectively, it has been decided that:

(i) In respect of the examinations to be conducted by the Institute for the period

February to July of a calendar year, instructions / guidelines issued by the regulator(s) and important developments in banking and finance up to 31st
December will only be considered for the purpose of inclusion in the question papers".

(ii) In respect of the examinations to be conducted by the Institute for the period

August to January of a calendar year, instructions / guidelines issued by the regulator(s) and important developments in banking and finance up to 30th June will only be considered for the purpose of inclusion in the question papers.

The table given below further clarifies the situation.

Particulars Developments for Examination/s	**Cut-off Date of Guidelines / Important Developments for Examination/s**
For the examinations to be conducted by the Institute for the period February 2018 to July 2018	31st December 2017
For the examinations to be conducted by the Institute for the period August 2018 to January 2019	30th June 2018

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SYLLABUS

I. a) FEDAI Role and Rules

b) Foreign Exchange Rates and Risk Management

c) Code of Conduct, Ethics / Compliance, Corporate Governance

II. Regulatory Requirements under FEMA for Resident / Non-resident Individuals

a) Remittance Facilities under LRS

b) Other Remittance Facilities for Resident indians / others

c) Various foreign currency accounts in india / Abroad

d) Acquisition of Assets, Immovable properties outside India, including investments in securities abroad

e) Remittance of Assets

f) Facilities for Non-resident Indians - Deposits Accounts, Investments, Borrowing etc.

III. Regulatory Requirements under FEMA for Resident / Non-resident Entities

a) Import of Goods & Services and other non-import remittance

b) External commercial borrowing

c) Export of goods and services

d) Investments outside India

e) Investments in India by non-resident Corporates / FPIs / Others Entities

f) Establishments of LO / BO / PO in India by foreign entities
IV. Documentary Credits & Standby Credits
a) ICC guidelines pertining to INCOTERMS 2010, URC 522

b) UCP 600, eUCP version 1.1

c) ISBP - ICC PUB. 745, URBO - ICC PUB. 750, URDG 758

d) DOCDEX Rules - ICC PUB. 872 V. Export Finance

a) Various finance available by way for Pre-shipment / Post-shipment finance in Rupes and Foreign Currency

b) International Factoring, Forfaiting

c) Export Credit Guarantee Corporatio (ECGC)
VI. Foreign Trade Policy (FTP) 2015-20
a) Various policy issues withspecific relevance to AD Banks with latest updations

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Foreign Exchange Dealers Association of India (FEDAI)

DEFINITION of 'Foreign Exchange Dealers Association of India (FEDAI)'
The Foreign Exchange Dealers Association of India (FEDAI) is an association of banks that specializes in the foreign exchange markets in India. (These institutions are also called Authorised Dealers or ADs.) Created in 1958, the body regulates the rules that determine commissions and charges that are attached to the interbank foreign exchange business.

BREAKING DOWN 'Foreign Exchange Dealers Association of India (FEDAI)'

FEDAI determines many of the rules that overlook the day-to-day forex transactions in India. In addition to rule setting, FEDAI assists member banks by acting as an advisor and assists with the training of personnel and accrediting foreign exchange brokers.

Additional core functions include:

Advising and supporting member banks with issues that arise in their dealings

Representing member banks on the Reserve Bank of India (or RBI)

Announcement of daily and periodical rates to member banks

As of December 2017, FEDAI member banks spanned the public sector, private sector, foreign banks, and co-operative banks and financial institutions, among others. The total count was 102.

Foreign Exchange Dealers Association Of India (FEDAI) and Self-Regulating Organizations (SROs)
The FEDAI is a self-regulating organization or SRO. SROs exist independently of national governments (such as FINRA in the United States) yet still have power to create and enforce industry regulations and standards. SROs place enormous emphasis on ethics and equality. SROs are non-governmental agencies, which can be helpful in industries, such as finance, that are international.

Additional examples of SROs include the Investment Dealers Association of Canada, and the National Association of Securities Dealers (NASD) in the United States.

FEDAI has grown in its role as a SRO in India and now plays a key role in stabilizing markets through its cooperation with the Reserve Bank of India and the Fixed Income Money Market and Derivatives Association of India (FIMMDA). FEDAI continues to work with its partners to develop customized products and adhere to international accounting and risk management standards.

Recent Updates from the Foreign Exchange Dealers Association of India (FEDAI)
In March 2018, FEDAI joined forces with Financial Benchmark India (a company formed to administer money market benchmarks rates), FIMMDA, and the Indian Banks' Association (IBA) to set benchmarks for Indian rupee interest rates and foreign exchange. FBIL began publishing these rates in April 2018. Rates were displayed daily starting March 19, 2018. The Clearing Corporation of India (CCIL) is set to act as the calculating agent.

Gist of Important FEDAI Rules

Rule 1: Hours of Business
1.1 The exchange trading hours for Inter-bank forex market in India would be from
9.00 a.m. to 5.00 p.m. No customer transaction should be undertaken by the
Authorised Dealers after 4.30 p.m. on any working day. 1.2 Cut-off time limit of 05.00 p.m. is not applicable for cross- currency transactions.
In terms of paragraph 7.1 of Internal Control Guidelines over Foreign Exchange
Business of Reserve Bank of India (February 2011), Authorised Dealers are
permitted to undertake cross-currency transactions during extended hours, provided
the Managements lay down the extended dealing hours. 1.3 For the purpose of Foreign Exchange business, Saturday will not be treated as
a working day. 1.4 "Known holiday" is one which is known at least 4 working days before the date. A holiday that is not a "known holiday" is defined as a "suddenly declared holiday". Rule 2: Export Transactions
2.1. Post-shipment Credit in Rupees
(c) Application of exchange rate: Foreign Currency bills will be
purchased/discounted/ negotiated at the Authorised Dealer's current bill buying rate
or contracted rate. Interest for the normal transit period and/or usance period shall
be recovered upfront simultaneously. (d) Crystallization and Recovery:
(ii) Authorized Dealers should formulate own policy for crystallization of foreign
currency liability into rupee liability, in case of non-payment of bills on the due
date. (iii) The policy in this regard should be transparently available to the customers. (iv) For crystallization into Rupee liability, the Authorised Dealer shall apply its TT
selling rate of exchange. The amount recoverable, thereafter, shall be the
crystallized Rupee amount along with interest and charges, if any.

(v) Interest shall be recovered on the date of crystallization for the overdue period
at the appropriate rate; and thereafter till the date of recovery of the
crystallized amount. (vi) Export bills payable in countries with externalization issues shall also be
crystallized as per the policy of the authorised dealer, notwithstanding receipt
of advice of payment in local currency. (d) Realization of Bills after crystallization: After receipt of advice of realization,
the authorised dealer will apply TT buying rate or contracted rate (if any) to convert
foreign currency proceeds. (e) Dishonor of bills: In case of dishonor of a bill before crystallization, the bank
shall recover:
(ii) Rupee equivalent amount of the bill and foreign currency charges at TT selling rate. (iii) Appropriate interest and rupee denominated charges. 2.2. Application of Interest
(c) Rate of interest applicable to all export transactions shall be as per the
guidelines of Reserve Bank of India from time to time. (d) Overdue interest shall be recovered from the customer, if payment is not received within normal transit period in case of demand bills and on/or before

notional due date/actual due date in case of usance bills, as per RBI directive. (e) Early Realization: In case of early realization, interest for the unexpired period
shall be refunded to the customer. The bank shall also pay or recover notional swap
cost as in the case of early delivery under a forward contract. 2.3. Normal Transit Period:
Concepts of normal transit period and notional due date are linked to concessional
interest rate on export bills. Normal transit period comprises the average period
normally reckoned from the date of negotiation/purchase/discount till the receipt of
bill proceeds.
It is not to be confused with the time taken for the arrival of the goods at the destination. Normal transit period for different categories of export business are laid down as below:
(c) Fixed Due Date: In the case of export usance bills, where due dates are fixed, or are reckoned from date of shipment or date of bill of exchange etc, the actual due
date is known. Therefore, in such cases, normal transit period is not applicable. (d) Bills in Foreign Currencies – 25 days
(e) Exports to Iraq under United Nations Guidelines – Max. 120 days
(g) Bills drawn in Rupees under Letters of Credit (L/C)
(i) Reimbursement provided at centre of negotiation - 3 days
(ii) Reimbursement provided in India at centre different from centre of
negotiation - 7 days
(iii) Reimbursement provided by banks outside India - 20 days
(iv) Exports to Russia under L/C where reimbursement is provided by RBI - 20 days. (h) Bills in Rupees not under Letter of Credit - 20 days
(i) TT reimbursement under Letters of Credit (L/C)
(i) Where L/C provides for reimbursement by electronic means - 5 days
(ii) Where L/C provides reimbursement claim after certain number of days
from the date of negotiation - 5 days + this additional period. 2.4. Substitution/Change in Tenor:
(o) In case of change in the usance of a bill, interest on post-shipment credit shall
be charged to the customer, as per RBI guidelines. In addition, the bank shall
charge or pay notional swap difference. Interest on outlay of funds for such
swaps shall also be recovered from the customer at rate not below base rate
of the bank concerned. (p) It is optional for banks to accept delivery of bills under a contract made for
purchase of a clean TT. In such cases, the bank shall recover/pay notional
swap difference for the relative cover. Interest at the rate not below base rate
of the bank would be charged on the outlay of funds. 2.5. Export Bills sent for collection:
(a) Application of exchange rates: The conversion of foreign currency proceeds of
export bills sent for collection or of goods sent on consignment basis shall be
done at prevailing TT buying rate or the forward contract rate, as the case
may be. The conversion to Rupee equivalent shall be made only after the
foreign currency amount is credited to the nostro account of the bank. (b) On receipt of credit advice/statement of nostro account and compliances of
guidelines, requirements of the Bank and FEMA, the Bank shall transfer funds
for the credit of exporter's account within two working days. (c) If the above stipulated time limit is not observed, the Bank shall pay compensation for the delayed period at the minimum interest rate charged on
export credit. Compensation for adverse movement of exchange rate, if any, shall also be paid as per the compensation policy of the bank.

Rule 3: Import Transactions
3.1 Application of exchange rate:
(a) Retirement of import bills - Exchange rate as per forward sale contract, if
forward contract is in place. Prevailing Bills selling rate, in case there is no
forward contract. (b) Crystallization of Import - same as above bill (vide para 3.3 below)
(c) For determination of stamp - As per exchange rate provided by the duty on
import bills authority concerned. 3.2. Application of Interest:
(a) Bills negotiated under import letters of credit shall carry commercial rate of
interest as applicable to banks' domestic advances from time to time. (b) Interest remittable on interest bearing bills shall be subject to the directive of
Reserve Bank of India in this regard. 3.3. Crystallization of Import Bill under Letters of Credit. Unpaid foreign currency import bills drawn under letters of credit shall be
crystallized as per the stated policy of the bank in this respect. Rule 4 Clean Instruments:
4.1. Outward Remittance: Outward remittance shall be effected at TT selling rate of
the bank ruling on that date or at the forward contract rate. 4.2. Encashment of foreign currency notes and instruments, Foreign currency
travelers' cheques, currency notes, foreign currency in prepaid card, debit/credit
card will be encashed at Authorised Dealer's option at the appropriate buying rate
ruling on the date of encashment. 4. 3. Payment of foreign inward remittance, Foreign currency remittance up to an
equivalent of USD 10,000/- shall be immediately converted into Indian Rupees. Remittance in excess of equivalent of USD 10,000 shall be executed in foreign
currency. The beneficiary has the option of presenting the related instrument for
payment to the executing bank within the period prescribed under FEMA. 4.4. The applicable exchange rate for conversion of the foreign currency inward
remittance shall be TT buying rate or the contracted rate as the case may be. 4.5. Compensation for delayed payment: Authorised Dealers shall pay or send
intimation, as the case may be, to the beneficiary in two working days from the date
of receipt of credit advice / nostro statement. In case of delay, the bank shall pay
the beneficiary interest @ 2 % over its savings bank interest rate. The bank shall
also pay compensation for adverse movement of exchange rate, if any, as per its

compensation policy

Rule 5 Foreign Exchange Contracts:
5.1. Contract amounts: Exchange contracts shall be for definite amounts and
periods. When a bill contract mentions more than one rate for bills of different
deliveries, the contract must state the amount and delivery against each such rate. 5.2. Option period of delivery: Unless the date of delivery is fixed and indicated in
the contract, the option period may be specified at the discretion of the customer
subject to the condition that such option period of delivery shall not extend beyond
one month. If the fixed date of delivery or the last date of delivery option is a known
holiday, the last date for delivery shall be the preceding working day. In case of
suddenly declared holidays, the contract shall be deliverable on the next working
day. Contracts permitting option of delivery must state the first and last dates of
delivery. For Example: 18th January to 17th February, 31st January to 29th Feb. 2012. “Ready” or “Cash” merchant contract shall be deliverable on the same day. “Value next day” contract shall be deliverable on the working day immediately
succeeding the contract date. A spot contract shall be deliverable on second
succeeding working day following the contract date. A forward contract is a contract
deliverable at a future date, duration of the contract being computed from spot value
date at the time of transaction”. 5. 3. Place of delivery: All contracts shall be understood to read “to be delivered or
paid for at the Bank” and “at the named place”. 5.4. Date of delivery: Date of delivery under forward contracts shall be:
(i) In case of bills/documents negotiated, purchased or discounted - the date of
negotiation/purchase/ discount and payment of Rupees to the customer. However, in case the documents are submitted earlier than, or later than the
original delivery date, or for a different usance, the bank may treat it as proper
delivery, provided there is no change in the expected date of realization of
foreign currency calculated at the time of booking of the contract. No early
realization or late delivery charges shall be recovered in such cases. (ii) In case of export bills/documents sent for collection - Date of payment of
Rupees to the customer on realization of the bills. (iii) In case of retirement/crystallization of import bills/documents - the date of retirement/ crystallization of liability, whichever is earlier?
5.5. Option of delivery: In all forward merchant contracts, the merchant, whether a
buyer or a seller will have the option of delivery. 5.6. Option of usance: The merchant purchase contract should state the tenor of the bills/documents. Acceptance of delivery of bills/documents drawn for a different
tenor will be at the discretion of the bank

5.7. Merchant quotations: The exchange rate shall be quoted in direct terms i.e. so many Rupees and Paise for 1 unit or 100 units of foreign currency. 5.8. Rounding off: Rupee equivalent of the foreign currency Settlement of all
merchant transactions shall be effected on the principle of rounding off the Rupee
amounts to the nearest whole Rupee i.e. without paise. RULE 6 Early Delivery, Extension and Cancellation of Foreign Exchange Contracts
6.1. General
(i) At the request of a customer, unless stated to the contrary in the provisions of
FEMA, 1999, it is optional for a bank to: (a). Accept or give early delivery; or
(b). Extend the contract. (ii) It is the responsibility of a customer to effect delivery or request the bank for
extension / cancellation as the case may be, on or before the maturity date of
the contract. 6.2. Early delivery: If a bank accepts or gives early delivery, the bank shall
recover/pay swap difference, if any. 6.3. Extension: Foreign exchange contracts where extension is sought by the
customers shall be cancelled (at an appropriate selling or buying rate as on the date
of cancellation) and rebooked simultaneously only at the current rate of exchange. The difference between the contracted rate, and the rate at which the contract is
cancelled, shall be recovered from/paid to the customer at the time of extension. Such request for extension shall be made on or before the maturity date of the
contract. 6.4. Cancellation
(i) In case of cancellation of a contract at the request of a customer, (the request
shall be made on or before the maturity date) the Authorised Dealer shall
recover/ pay, as the case may be, the difference between the contracted rate
and the rate at which the cancellation is effected. The recovery/payment of
exchange difference on cancellation of forward contracts before the maturity
date may be either upfront or back-ended at the discretion of banks. (ii) Rate at which cancellation is to be effected:
(a) Purchase contracts shall be cancelled at T.T. selling rate of the
contracting Authorised Dealer
(b) Sale contracts shall be cancelled at T.T. buying rate of the contracting
Authorised Dealer

(c) Where the contract is cancelled before maturity, the appropriate forward
T.T. rate shall be applied. (bi) Notwithstanding the fact that the exchange contract between the customer
and the bank becomes impossible of performance, for whatever reason,
including Government prohibitory orders, the exchange contract shall not be
deemed to have become void and the customer shall forthwith apply to the
Authorised Dealer for cancellation, as per the provisions of paragraph 6.4.(i)
and (ii) above. (iv)
(d) In the absence of any instructions from the customer, vide para 6.1(ii), a
contract which has matured shall be cancelled by the bank on the 7th working
day after the maturity date. (e) Swap cost, if any, shall be recovered from the customer under advice to him. © When a contract is cancelled after the maturity date, the customer shall not be entitled

to the exchange difference, if any, in his favour, since the contract is cancelled on account of his default. He shall, however, be liable to pay the exchange difference against him. 6.5. Swap cost/gain:
(ii) In all cases of early delivery of a contract, swap cost shall be recovered from the customer, irrespective of whether an actual swap is made or not. Such recoveries should be made either back-ended or upfront at discretion of the bank. (iii) Payment of swap gain to a customer shall be made at the end of the swap period. 6.6. Outlay and Inflow of funds: Authorised Dealer shall recover interest on outlay of funds for the purpose of arranging the swap, in addition to the swap cost in case of early delivery of a contract.
If such a swap leads to inflow of funds, interest shall be paid to the customer. Funds outlay / inflow shall be arrived at by taking the difference between the original contract rate and the rate at which the swap could be arranged. The rate of interest to be recovered / paid should be determined by banks as per their policy in this regard.

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Main Features of the Foreign Exchange Management Act (FEMA)

The Foreign Exchange Management Act (FEMA) was an act passed in the winter session of Parliament in 1999, which replaced Foreign Exchange Regulation Act. This act seeks to make offences related to foreign exchange civil offences. It extends to the whole of India.

The Foreign Exchange Regulation Act (FERA) of 1973 in India was replaced on June 2000 by the Foreign Exchange Management Act (FERA), which was passed in 1999. The FERA was passed in 1973 at a time when there was acute shortage of foreign exchange in the country.

It had a controversial 27 years stint during which many bosses of the Indian corporate world found themselves at the mercy of the Enforcement Directorate. Moreover, any offence under FERA was a criminal offence liable to imprisonment. But FEMA makes offences relating to foreign civil offences.

FEMA had become the need of the hour to support the pro- liberalisation policies of the Government of India. The objective of the Act is to consolidate and amend the law relating to foreign exchange with the objective of facilitating external trade and payments for promoting the orderly development and maintenance of foreign exchange market in India.

FEMA extends to the whole of India. It applies to all branches, offices and agencies outside India owned or controlled by a person, who is a resident of India and also to any contravention there under committed outside India by two people whom this Act applies.

The Main Features of the FEMA:

The following are some of the important features of Foreign Exchange Management Act:

i. It is consistent with full current account convertibility and contains provisions for progressive liberalisation of capital account transactions.

ii. It is more transparent in its application as it lays down the areas requiring specific permissions of the Reserve Bank/Government of India on acquisition/holding of foreign exchange.

iii. It classified the foreign exchange transactions in two categories, viz. capital account and current account transactions.

iv. It provides power to the Reserve Bank for specifying, in , consultation with the central government, the classes of capital account transactions and limits to which exchange is admissible for such transactions.

v. It gives full freedom to a person resident in India, who was earlier resident outside India, to hold/own/transfer any foreign security/immovable property situated outside India and acquired when s/he was resident.

vi. This act is a civil law and the contraventions of the Act provide for arrest only in exceptional cases.

vii. FEMA does not apply to Indian citizen's resident outside India.

Difference between the FERA and FEMA:

FERA, 1973	FEMA, 1999
It is an old enactment. It was passed in 1973. Now this Act has been repeated.	It is a new enactment. It was passed in the year 1999.
It was a long enactment with 81 Sections. It was very strict in nature.	It is a small enactment with 49 Sections. It is liberal in nature.
Approach towards foreign exchange transactions was very conservative and restrictive.	The approach towards foreign exchange transactions is very positive and welcoming.
Penalty provisions were very hard. In this Act, imprisonment was imparted to the person violating its provisions.	It provides only for monetary penalty for violating the provisions. Imprisonment is imparted only on non-payment of monetary penalty.
The scope of FERA was very wide. It dealt with all the transactions related to foreign exchange, i.e, anything and everything related to foreign exchange was controlled by FERA.	The scope of FEMA is narrow. It deals only with specified transactions related to foreign exchange, i.e. it checks and controls only those transactions, which are specifically mentioned in the Act. It dose not deal with the transactions which are not specifically mentioned in its scope.

4 Main Participants of Foreign Exchange Market

The participants are: 1. Commercial Banks or Market Makers 2. Foreign Exchange Brokers 3. Central Banks or Reserve Bank of India 4. Corporates and Entrepreneurs.

Participant # 1. Commercial Banks or Market Makers:
Commercial banks are normally taking over the position to support the economy of the country by carrying over the foreign currency from one period to another, for meeting the future need of the country. They are also sometime making short sale (agree to sell or actually sell the foreign currency without any real capacity to sell through or borrow the required currency from others) of foreign currency to satisfy the need of firms to make payments.

Later on to bring the position in equilibrium, they quote the rates for buying and selling of foreign currency accordingly. As they are buying the foreign currency from the customer, the rate they quote for buying the foreign currency is technically named as Bid rate. When they sell the foreign currency to customer, the rate they quote is technically known as Ask rate.

Participant # 2. Foreign Exchange Brokers:
ADVERTISEMENTS:

FE brokers do not buy or sell the foreign currency on their own account, as done by market makers. They are working as an intermediary between two parties, to satisfy their respective needs. As they are working as a bridge between buyers and sellers of the foreign currency, they are only earning the fees in the form of brokerage charges.

Participant # 3. Central Banks or Reserve Bank of India:
To protect the financial strength and stability of the country's balance of payments, internal money supply, interest rates and inflation, RBI intervenes in the foreign exchange markets to protect the disequilibrium in the prices of foreign exchange conversion.

Participant # 4. Corporates and Entrepreneurs:
Corporate are the players in the FE market, to satisfy their need of payment in foreign currency towards imports of goods, commodities and services. On the opposite way, they need to convert foreign currency in home currency on account of export of goods, commodities, and services. The need of conversion also happens on account of transactions in financial markets across the globe, for loan disbursement, repayment of loans, receipt and payment of annual charges, etc.

Provisions of Foreign Exchange Management Act

Provisions of Foreign Exchange Management Act (FEMA) provides free transaction on current account subject to the guidelines by the RBI. Enforcement of Foreign Exchange Management Act (FEMA) is entrusted to a separate directorate, which undertakes investigations on contraventions of the Act.

Provisions of FEMA are grouped under four heads. Important provisions under each of the four heads, having a bearing on promoting economic development through foreign investment with enabling provisions to ensure the curtailing of inflationary trends from such transactions, are outlined below.

Regulation for Current Account Transaction:

Any person can sell or draw foreign exchange to or from an authorised dealer (if such sale or withdrawal is a current account transaction) except for certain prohibited transactions like remittance of lottery winnings, remittance of interest income on funds held in Non-Resident Special Rupee (NRSR) account scheme, etc.

Besides these cases, there are certain other transactions, for which specific RBI approval will be required. For instance, Reserve Bank approval is required for importers availing of Supplier's Credit beyond 180 days and Buyer's Credit irrespective of the period of credit.

Authorised dealers are permitted remittance of surplus freight/passage collections by shipping/airline companies or their agents, multimodal transport operators, etc. after verification of documentary evidence in support of the remittance.

Regulations Relating to Capital Account Transactions:

i. Foreign nationals are not allowed to invest in any company or partnership firm or proprietary concern, which is engaged in the business of Chit Fund or in Agricultural or Plantation activates or in Real Estate business (other than development of township, construction of residential/commercial premises, roads or bridges) or construction of farm houses or trading in Transferable Development Rights (TDRs). Listing of permissible classes of Capital account transaction for a person resident in India and also by a person resident outside India has been provided in the regulations.

ii. Detailed rules and regulations are provided on borrowing and lending in Foreign Currency as well as India Rupee by a person resident in India form/to a person resident outside India either on non-repatriation or repatriation basis.

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iii. Authorised dealers are now permitted to grant rupee loans to NRIs against security of shares or immovable property in India, subject to certain terms and conditions. Authorised dealers or housing finance institutions approved by National Housing Bank can also grant rupee loans to NRIs for acquisition of residential accommodations subject to certain terms and conditions.

iv. General permission has been granted to Indian company (including Non-Banking Finance Company) registered with Reserve Bank to accept deposits from NRIs on repatriation basis subject to the terms and conditions specified in the schedule.

Indian proprietorship concern/firm or a company (including Non-Banking Finance Company) registered with Reserve Bank can also accept deposits from NRIs on non-repatriation basis subject to the terms and conditions specified in the schedule.

Regulations relating to export of goods and services:

Export proceeds are required to be realised within a period of 6 months from the date of shipment. In the case of exports to a warehouse established abroad with the approval of Reserve Bank, the proceeds have to be realised within 15 months from the date of shipment.

An enabling provision has been made in this regulation to delegate powers to authorised dealers to allow extension of time. Export of goods on elongated credit terms beyond six months requires prior approval of Reserve Bank.

Other Regulations:

i. A person resident in India to whom any foreign exchange is due or has accrued is obligated to take reasonable steps to realise and repatriate to India such foreign exchange unless an exemption has been provided in the Act or regulations made under the general or special permission of Reserve Bank.

ii. Any foreign exchange due or accrued as remuneration for services rendered or in settlement of any lawful obligation or an income on assets held outside India or as inheritance, settlement or gift to a person resident in India should be sold to an authorised person within a period of seven days of its receipt and in all other cases within 90 days of its receipt.

iii. Any person who has drawn exchange for any purpose but has not utilised it for the same or any other purpose permissible under the provisions of the Act should surrender such foreign exchange or un-utilised foreign exchange to an authorised person within a period of 60 days from the date of acquisition.

Where, however, exchange was drawn for travel abroad, the un-utilised exchange in excess of the limit up to which foreign exchange is permitted to be retained, should be surrendered to an authorised person within 90 days from the date of return of the' traveller to India if unspent exchange is in the form of travellers cheques.

iv. The Reserve Bank has specified the limit for possession and retention of foreign currency by a person resident in India. There is no restriction on possession of foreign coins by any person. Any person resident in India is permitted to retain in aggregate foreign currency not exceeding US$ 2000 or its equivalent in the form of currency notes/bank notes or travellers cheques acquired by him from approved sources.

v. The Reserve Bank has granted general permission to any person to receive any payment:

(a) made in rupees by order or on behalf of a person resident outside India during his stay in India by converting the foreign exchange into rupees by sale to an authorised person;

(b) made by means of a cheque drawn on a bank outside India or a bank draft or travellers cheques issued outside India or made in foreign currency notes directly, provided the cheques, drafts or foreign currency is sold to an authorised person within seven days of its receipt;

(c) by means of a postal order or money order issued by a post office outside India.

vi. Reserve bank has also granted general permission to a person resident in India to make payment in rupees;

(a) for extending hospitality' to a person resident outside India;

(b) to a person resident outside India for purchase of gold or silver imported by such person in accordance with the provisions of any order issued by Central Government under the Foreign Trade (Development and Regulation) Act, 1992 or under any law or rules or regulations in force.

OVERVIEW OF FOREIGN EXCHANGE MANAGEMENT ACT

BACKGROUND – EVOLUTION OF FOREIGN EXCHANGE REGULATIONS IN INDIA
Exchange regulations have always remained at the centre of Indian economy. Exchange controls were first introduced in India during the Second World War (1942). Soon after independence, they were formally reaffirmed in form of the first Foreign Exchange Regulation Act, 1949 (FERA). This was followed by FERA, 1973. The control framework under FERA was essentially transaction based in terms of which all transactions in foreign exchange including those between residents to nonresidents were prohibited unless specifically permitted.
Transformation from control-to-management: FERA to FEMA

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The 1970s and 1980s saw the rise of large external sector imbalances on account of persistent increase in adverse balance of payments situation. There was over dependence on official foreign aid. It was this balance of payment crisis that triggered the wave of economic liberalization. The Indian rupee became market determined in 1993. The need was felt to consolidate and amend the law relating to foreign exchange with the objectives of facilitating external trade and payments and for promoting the orderly development and maintenance of foreign exchange market in India. Accordingly, on June 1, 2000, the Foreign Exchange Management Act, 1999 (FEMA) was brought in force to replace the then existing Foreign Exchange Regulation Act, 1973 (FERA). FEMA has been enacted with an objective of facilitating external trade and payments and for promoting the orderly development and maintenance of foreign exchange market tin India. As such it is quite opposed to FERA which was enacted to regulate or control the foreign exchange. FEMA provided a de jure status to the shift in policies with regard to the external sector reforms that began in 1990-91.
STRUCTURE OF FEMA
The present framework of exchange controls in India, consist of basic legislation (FEMA, 1999) and Notifications, Rules and Circulars [known as Authorized Persons Directions – AP (Dir Series)] issued by RBI. 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. It also applies to any contraventions committed outside India by any person to whom FEMA applies.
There are 49 sections under FEMA, of which 9 sections (section 1 to 9) are substantive and the rest are procedural / administrative provisions as tabulated below:
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 and Directorate of Enforcement
39 to 49 Miscellaneous Provisions
Section 46 of FEMA grants power to the Central Government to make rules to carry out the provisions of FEMA and Section 47 of FEMA grants power to the Reserve Bank of India (RBI) to make regulations to implement provisions and the rules made under FEMA. Thus RBI is entrusted with the administration and implementation of FEMA.
CAPITAL ACCOUNT TRANSACTION AND CURRENT ACCOUNT TRANSACTION:
In August 1994 India accepted Article VIII of the Articles of agreement of the International Monetary Fund and became fully convertible on the current account. Since India is fully convertible on the current account, all current account transactions (barring a small list of restricted items) are allowed through the normal banking channels. In case of capital account transactions, only the transactions which are explicitly enabled under the guidelines are allowed, remaining require specific approvals under FEMA.
Accordingly it is very important to understand the concept of Capital and Current Account Transactions to Comprehend FEMA.
A. Capital Account Transaction:
"Capital Account transaction" is defined under section 2(e) of FEMA as '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, and includes transactions referred to in sub-section (3) of section 6.'
Thus any transaction as a result of which the assets or liabilities outside India of a person who is resident in India and assets or liabilities in India of a person who is resident outside India are altered i.e. either increased or decreased, is a capital account transaction.
To put it in example, if a person resident in India acquires shares of a foreign company, his/her overseas assets will increase. Similarly, if the same person borrows from a non resident through External Commercial Borrowings (ECBs) his/her liability is created outside India. Hence, both the transactions lead to creation of asset or liability outside India of a person resident in India. Both the transactions are capital account transactions.
In case of a person resident outside India, if he acquires shares of an Indian company, his/her asset is created in India and if same person borrows from an institution in India for acquiring house in India, his/her liability will be created in India. Both these transactions lead to creation of asset or liability in India of a person resident outside India. Hence, both the transactions are capital account transactions.
The concept of Capital and Current Account transaction is to be seen from Balance of Payment point of view. If after the completion of transaction there remains any obligation to either pay or receive foreign exchange, the transaction would get colour of Capital Account transaction.
For example, import of Plant & Machinery is a current account transaction, as upon import the machinery is received in India and overseas supplier is say paid within six months from import and accordingly there is no future obligation on India as a country to honour foreign exchange obligation. In this example, from accounting perspective, though Plant & Machinery would be capital goods, but for FEMA it would be a current account transaction.
RBI has been empowered under section 6(2) of FEMA to specify, in consultation with the Central Government, any class or classes of Capital Account transactions which are permissible [i.e. over and above the transactions permitted under section 6(3)]. Section 6(3) of FEMA specifies the classes of capital account transactions which are regulated by RBI. Every transaction listed in this section is regulated by a corresponding notification/regulation.

FEMA Notification No. 1/2000-RB dated 3-5-2000 contains the list of permissible capital account transactions as well as list of prohibited capital account transactions.

Prohibited Capital Account Transactions:
General Prohibition:
A person shall not undertake or sell or draw foreign exchange to or from an Authorized person for any capital account transactions other than those permitted in the Schedules, provided the transaction is within the limit.
Special Prohibition:
No person resident outside India shall make investment 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-

- In the business of chit fund, or
- As nidhi company, or
- In agricultural or plantation activities, or
- In real estate business, or construction of farm houses, or
- In trading in Transferable Development Rights (TDRs)

(real estate shall not include development of townships, construction of residential/commercial premises, roads or bridges).
B. Current Account Transaction:
"Current account transaction" is defined under section 2(j) of FEMA to mean 'a transaction other than a capital account transaction and without prejudice to the generality of the foregoing such transaction includes,-
(i) payments due in connection with foreign trade, other current business, services and shortterm 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 parent, spouse and children residing abroad, and
(iv) expenses in connection with foreign travel, education and medical care of parents, spouse and children.'
All Current Account transactions are generally permitted unless specifically prohibited whereas all Capital Account transactions are generally prohibited unless specifically permitted.
Current Account transactions are divided into 3 schedules in Current Account Transaction rules:
Schedule I – Prohibited Transactions
Schedule II – Transactions requiring prior approval of Government of India
Schedule III – Transactions requiring prior approval of RBI
EXAMPLES TO UNDERSTAND CAPITAL AND CURRENT ACCOUNT TRANSACTIONS:
a. Import of Machinery on hire purchase:
In this transaction the person has created future obligation for making payment to nonresident and hence has liability towards the non-resident. Therefore the said transaction is a capital account transaction.
b. Transaction representing creation or acquisition of wealth, shares, loans or immovable properties:
Since such types of transactions would lead to creation of assets in or outside India by person resident outside or in India, as the case may be, the same are in nature of capital account transactions.
c. Remittances out of winnings from lottery:
This comes under Prohibited list (Schedule I) of the Current account transaction. Hence although the same is in nature of current account such transactions are prohibited.
However, an entity engaged in lottery business, imports any software or machinery to be utilized in lottery business in India, the same is a permissible transaction. Import of software or machinery will not result in violation of FEMA regulations in relation to current account transactions.
But any type of technical collaboration for lottery business including licensing for franchise, trademark, brand name, management contract or any contract for payment of royalty as such for such collaboration is prohibited under both current account transaction rules and also under FDI Policy. Hence, such transactions are not permissible.
d. Options premium payable under NASDAQ:
Options premium is the price paid by a person to buy an option contract, whether it is a call or put. So option premium is paid to acquire only specified rights for a contract. Under option contract there is no future obligation in addition to option premium paid at the time of entering into contract so it does not result into creation of any contingent liability and hence is a current account transaction. Whereas future contract would be a capital account transaction. Option contract may result into creation of contingent asset, and such contingent asset is not covered in the definition of Capital Account transaction.
e. Opening a branch outside India:
Opening a branch outside India is a current account transaction as it does not result into alteration of any assets and liabilities overseas, since overseas branch would be regarded as Resident of India. If however, such overseas branch proposes to acquire immovable property (say office premises) outside India, such acquisition would be regarded as Capital Account Transaction.
Opening a branch outside India is a permissible current account transaction and regulated by Notification No. 10/2000-RB dated 3-5-2000 dealing with Foreign Currency accounts by a person resident in India.
OTHER IMPORTANT SECTIONS – SEC 6(4) AND SEC 6(5):
Section 6(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,

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held or owned by such person when he was resident outside India or inherited from a person who was resident outside India.
However, there was no clarity on the type of transactions that would be covered under section 6(4). Hence, RBI with a view to resolve the doubts, vide its A. P. (DIR Series) Circular No. 90 dated January 9, 2014 clarified that the following transactions shall be covered under Section 6(4) of FEMA, 1999:
a. Foreign currency accounts opened and maintained by such a person when he was resident outside India.
b. Income earned through employment or business or vocation outside India taken up or commenced, or from investments made, or from gift or inheritance received while such a person was resident outside India.
c. Foreign exchange including any income arising there from, and conversion or replacement or accrual to the same, held outside India acquired by way of inheritance from a person resident outside India.
d. 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 prior approval of RBI
Thus, section 6(4) gives liberty to a person resident in India to keep with him any foreign currency or foreign security or immovable property which he might have acquired when he was resident outside India, without any compliance and reporting under FEMA.
Section 6(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 such person when he was resident in India or inherited from a person who was resident in India.
This section allows a person resident outside India to keep with him any currency, security or immovable property which he might have acquired when he was resident in India. In case if the person liquidates his investment owned by him in India, he can keep the funds in his NRO account. RBI vide Notification 13 (Remittance of assets) allows to remit the balances of sales proceeds of assets held by NRI subject to the limit of USD 1 million per financial year.

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THE FOREIGN EXCHANGE MANAGEMENT ACT, 1999
ACT NO. 42 OF 1999 [29th December, 1999.]

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.
BE it enacted by Parliament in the Fiftieth Year of the Republic of India as follows:-

• PRELIMINARY
Short title, extent, application and commencement.
• This Act may be called the Foreign Exchange Management Act, 1999.
• It extends to the whole of India.
• 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 outs ide India by any person to whom this Act applies .
• It shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint: Provided that different dates may be appointed for different provisions of this Act and any reference in any such provision to the commencement of this Act shall be construed as a reference to the coming into force of that provision.
Definitions
• Definitions.-In this Act, unless the context otherwise requires,- (a) "Adjudicating Authority" means an officer authorized under sub-section (1) of section 16
• "Appellate Tribunal" means the Appellate Tribunal for Foreign Exchange established under section 18;
• "authorized person" means an authorized dealer, money changer, off-shore banking unit or any other person for the time being authorized under subsection (1) of section 10 to deal in foreign exchange or foreign securities;
• "Bench" means a Bench of the Appellate Tribunal;
• "capital account transaction" 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, and

includes t ansactions referred to in sub-section (3) of section 6;
• "Chairperson" means the Chairperson of the Appellate Tribunal;
• "chartered accountant" shall have the meaning assigned to it in clause (b) of sub-section (1) of section 2 of the Chartered Accounts Act, 1949 (38 of 1949);
• "currency" includes all currency notes, postal notes, postal orders, money orders, cheques, drafts, travelers 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" means and includes cash in the form of coins and bank notes;
• "current account transaction" means a transaction other than a capital account transaction and without prejudice to the generality of the foregoing such transaction includes,-
o payments due in connection with foreign trade, other current business, services, and short-term banking and credit facilities in the ordinary course of business,
o payments due as interest on loans and as net income from investments,
o remittances for living expenses of parents, spouse and children residing abroad, and
o expenses in connection with foreign travel, education and medical care of parents, spouse and children;
• "Director of Enforcement" means the Director of Enforcement appointed under sub-section (1) of section 36;
o "export", with its grammatical variations and cognate expressions, meanso
the taking out of India to a place outside India any goods,
o provision of services from India to any person outside India;
• "foreign currency" means any currency other than Indian currency;
• "foreign exchange" means foreign currency and includes,-
o deposits, credits and balances payable in any foreign currency
o drafts, travelers cheques, letters of credit or bills of exchange, expressed or drawn in Indian currency but payable in any foreign currency,
o drafts, travelers cheques, letters of credit or bills of exchange drawn by banks, institutions or persons outside India, but payable in Indian currency;
• "foreign security" means 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 where redemption or any form of re urn such as interest or dividends is payable in Indian currency;
• "import", with its grammatical variations and cognate expressions, means bringing into India any goods or services;
• "Indian currency" means currency which is expressed or drawn in Indian rupees but does not include special bank notes and special one rupee notes issued under section 28A of the Reserve Bank of India Act, 1934 (2 of 1934);
• "legal practitioner" shall have the meaning assigned to it in clause (i) of subsection (1) of section 2 of the Advocates Act, 1961 (25 of 1961);
• "Member" means a Member of the Appellate Tribunal and includes the Chairperson thereof;
• "notify" means to notify in the Official Gazette and the expression "notification" shall be construed accordingly;
• "person" includeso
an individual,
o a Hindu undivided family,
o a company,
o a firm,
o an association of persons or a body of individuals, whether incorporated or not,
o every artificial juridical person, not falling within any of the preceding sub-clauses, and
o any agency, office or branch owned or controlled by such person;
• "person resident in India" means- (i) a person residing in India for more than one hundred and eighty-two days during the course of the preceding financial year but does not includeo
a person who has gone out of India or who stays outside India, in either case-
for or on taking up employment outside India, or
for carrying on outside India a business or vocation outside India, or
for any other purpose, in such circumstances as would indicate his intention to stay outside India for an uncertain period;
o a person who has come to or stays in India, in either case, otherwise than-
for or on taking up employment in India, or
for carrying on in India a business or vocation in India, or

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o (i) for any other purpose, in such circumstances as would indicate his intention to stay in India for an uncertain period;
any person or body corporate registered or incorporated in India
an office, branch or agency in India owned or controlled by a person resident outside India,
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;
• "prescribed" means prescribed by rules made under this Act;
• "repatriate to India" means bringing into India the realized foreign exchange ando
the selling of such foreign exchange to an authorized person in India in exchange for rupees, or
o the holding of realized amount in an account with an authorized person in India to the extent notified by the Reserve Bank, and includes use of the realized amount for discharge of a debt or liability denominated in foreign exchange and the expression "repatriation" shall be construed accordingly;
• "Reserve Bank" means the Reserve Bank of India constituted under subsection (1) of section 3 of the Reserve Bank of India Act, 1934 (2 of 1934);
o "security" means shares, stocks, bonds and debentures, Government securities as defined in the Public Debt Act, 1944 (18 of 1944), savings certificates to which the Government Savings Certificates Act, 1959 (46 of 1959) applies, deposit receipts in espect of deposits of securities and units of the Unit Trust of India established under sub-section (1) of section 3 of the Unit Trust of India Act, 1963 (52 of 1963) or of any mutual fund and includes certificates of title to securities, but does not in lude bills of exchange or promissory notes other than Government promissory notes or any other instruments which may be notified by the Reserve Bank as security for the purposes of this Act;
o "service" means service of any description which is made available to potential users and includes the provision of facilities in connection with banking, financing, insurance, medical assistance, legal assistance, chit fund, real estate, transport, processing, supply of electrical or other energy, boarding or lodging or both, entertainment, amusement or the purveying of news or other information, but does not include the rendering of any service free of charge or under a contract of personal servic ;
o "Special Director (Appeals)" means an officer appointed under section 18;
o "specify" means to specify by regulations made under this Act and the expression "specified" shall be construed accordingly;
o "transfer" includes sale, purchase, exchange, mortgage, pledge, gift, loan or any other form of transfer of right, title, possession or lien.
CHAP
REGULATION AND MANAGEMENT OF FOREIGN EXCHANGE
CHAPTER II-REGULATION AND MANAGEMENT OF FOREIGN EXCHANGE
Dealing in foreign exchange, etc.
Dealing in foreign exchange, etc.-Save as otherwise provided in this Act, rules or regulations made thereunder, or with the general or special permission of the Reserve Bank, no person shall-
• deal in or transfer any foreign exchange or foreign security to any person not being an authorized person;
• make any payment to or for the credit of any person resident outside India in any manner;
• receive otherwise 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 inwa d remittance from any place outside India, then, such person shall be deemed to have received such payment otherwise than through an authorized person;
• 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. 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 r promissory note, or transferring any security or acknowledging any debt.
Holding of foreign exchange, etc.
Holding of foreign exchange, etc.-Save as otherwise 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.

Current account transactions.
Current account transactions.-Any person may sell or draw foreign exchange to or from an authorized person if such sale or drawal is a current account transaction: Provided that the Central Government may, in public interest and in consultation with the Reserve Bank, impose such reasonable restrictions for current account transactions as may be prescribed
Capital account transactions.
• 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.
• The Reserve Bank may, in consultation with the Central Government, specifyo any class or classes of capital account transactions which are permissible;
o the limit up to which foreign exchange shall be admissible for such transactions: Provided that the Reserve Bank shall not impose any restriction on the drawal of foreign exchange for payments due on account of amortization of loans or for depreciation of direct investments in the ordinary courts of business.
• Without prejudice to the generality of the provisions of sub-section (2), the Reserve Bank may, by regulations, prohibit, restrict or regulate the followingo transfer or issue of any foreign security by a person resident in India;
o transfer or issue of any security by a person resident outside India;
o transfer or issue of any security or foreign security by any branch, office or agency in India of a person resident outside India;
o any borrowing or lending in rupees in whatever form or by whatever name called;
o any borrowing or lending in rupees in whatever form or by whatever name called between a person resident in India and a person resident outside India;
o deposits between persons resident in India and persons resident outside India;
o export, import or holding of currency or currency notes;
o transfer of immovable property outside India, other than a lease not exceeding five years, by a person resident in India;
o acquisition or transfer of immovable property in India, other than a lease not exceeding five years, by a person resident outside India;
o 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.
• 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.
• 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.
• 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.
Export of goods and services.
• Every exporter of goods shallo
furnish to the Reserve Bank or to such other authority a declaration in such form and in such manner as may be specified, containing true and correct material particulars, including the amount representing the full export value or, if the full export value of the goods is not ascertainable at the time of export, the value which the exporter, having regard to the prevailing market conditions, expects to receive on the sale of the goods in a market outside India;
o furnish to the Reserve Bank such other information as may be required by the Reserve Bank for the purpose of ensuring the realization of the export proceeds by such exporter.
• The Reserve Bank may, for he purpose of ensuring that the full export value of the goods or such reduced value of the goods as the Reserve Bank determines, having regard to the prevailing market conditions, is received without any delay, direct any e porter to comply with such requirements as it deems fit.
• Every exporter of services shall furnish to the Reserve Bank or to such other authorities a declaration in such form and in such manner as may be specified, containing the true and correct material particulars in relation to payment for

such services
Realisation and repatriation of foreign exchange.
Realisation and repatriation of foreign exchange.-Save as otherwise provided in this Act, where any amount of foreign exchange is due or has accrued to any person resident in India, such person shall take all reasonable steps to realize and repatriate to India such foreign exchange within such period and in such manner as may be specified by the Reserve Bank.
Exemption from realization and repatriation in certain cases.
Exemption from realization and repatriation in certain cases. -The provisions of sections 4 and 8 shall not apply to the following, namely:-
• possession of foreign currency or foreign coins by any person up to such limit as the Reserve Bank may specify;
• foreign currency account held or operated by such person or class of persons and the limit up to which the Reserve Bank may specify;
• foreign exchange acquired or received before the 8th day of July, 1947 or any income arising or accruing thereon which is he ld outside India by any person in pursuance of a general or spec ial permission granted by the Reserve Bank;
• foreign exchange held by a person resident in India up to su ch limit as the Reserve Bank may specify, if such foreign exchan ge was acquired by way of gift or inheritance from a person refe rred to in clause (c), including any income arising therefrom;
• foreign exchange acquired from employment, business, trade, vocation, services, honorarium, gifts, inheritance or any other legitimate means up to such limit as the Reserve Bank may specif y; and
• such other receipts in foreign exchange as the Reserve Bank may specify.
CHAP
AUTHORISED PERSON
CHAPTER III- AUTHORISED PERSON
Authorised person.
• The Reserve Bank may, on an application made to it in this behalf, authorize any person to be known as authorized person to deal in foreign exchange or in foreign securities, as an authorized dealer, money changer or off-shore anking unit or in any other manner as it deems fit.
• An authorization under this section shall be in writing and shall be subject to the conditions laid down therein.
• An authorization granted under sub-section (1) may be revoked by the Reserve Bank at any time if the Reserve Bank is satisfied thato
it is in public interest so to do; or
o the authorized person has failed to comply with the condition subject to which the authorization was granted or has contravened any of the provisions of the Act or any rule, regulation, notification, direction or order made thereunder:
Provided that no such authorization shall be revoked on any ground referred to in clause (b) unless the authorized person has been given a reasonable opportunity of making a representation in the matter.
• An authorized person shall, in all his dealings in foreign exchange or foreign security, comply with such general or special directions or orders as the Reserve Bank may, from time to time, think fit to give, and, except with the previous permission f the Reserve Bank, an authorized person shall not engage in any transaction involving any foreign exchange or foreign security which is not in conformity with the terms of his authorization under this section.
• An authorized person shall, before undertaking any transaction in foreign exchange on behalf of any person, require that person to make such declaration and to give such information as will reasonably satisfy him that the transaction will not involve and is not designed for the purpose of any contravention or evasion of the provisions of this Act or of any rule, regulation, notification, direction or order made thereunder, and where the said person refuses to comply with any such requirement or make only unsatisfactory compliance therewith, the authorized person shall refuse in writing to undertake the transaction and shall, if he has reason to believe that any such contravention or evasion as aforesaid is contemplated by the person, report the mat er to the Reserve Bank.
• Any person, other than an authorized person, who has acquired or purchased foreign exchange for any purpose mentioned in the declaration made by him to authorized person under sub-section (5) does not use it for such purpose or does not surrender it o authorized person within the specified period or uses the foreign exchange so acquired or purchased for any other purpose for which purchase or acquisition or foreign exchange is not permissible under the provisions of the Act or the rules or regulatio s or direction or order made thereunder shall be deemed to have committed contravention of the provisions of the Act for the purpose of this section.
Reserve Bank's powers to issue directions to authorized person.
• Reverve Bank's powers to issue directions to authorized person.-(1) The Reserve Bank may, for the purpose of securing compliance with the provisions

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of this Act and of any rules, regulations, notifications or directions made thereunder, give to the a thorized persons any direction in regard to making of payment or the doing or desist from doing any act relating to foreign exchange or foreign security.
• The Reserve Bank may, for the purpose of ensuring the compliance with the provisions of this Act or of any rule, regulation, notification, direction or order made thereunder, direct any authorized person to furnish such information, in such manner, a it deems fit.
• Where any authorized person contravenes any direction given by the Reserve Bank under this Act or fails to file any return as directed by the Reserve Bank, the Reserve Bank may, after giving person a penalty which may extend to ten thousand rupees and in the case of continuing contravention with an additional penalty which may extend to two thousand rupees for every day during which such contravention continues. reasonable opportunity of being heard, impose on the author sed
Power of Reserve Bank to inspect authorised person.
• The Reserve Bank may, at any time, cause an inspection to be made, by any officer of the Reserve Bank specially authorised in writing by the Reserve Bank in this behalf, of the business of any a thorised person as may appear to it to be necessary or expedient for the purpose ofo
verifying the correctness of any statement, information or particulars furnished to the Reserve Bank;
o obtaining any information or particulars which such authorised person has failed to furnish on being called upon to do so;
o securing compliance with the provisions of this Act or of any rules, regulations, directions or orders made thereunder.
• It shall be the duty of every authorised person, and where such person is a company or a firm, every director, partner or other officer of such company or firm, as the case may be, to produce to any officer making an inspection under sub-section (1), such books, accounts and other documents in his custody or power and to furnish any statement or information relating to the affairs of such person, company or firm as the said officer may require within such time and in such manner as the said officer m y direct.

CONTRAVENTION AND PENALTIES

CHAPTER IV-CONTRAVENTION AND PENALTIES

Penalties
• If any person contravenes any provision of this Act, or contravenes any rule, regulation, notification, direction or order issued in exercise of the powers under this Act, or contravenes any condition subject to which an authorization s issued by the Reserve Bank, he shall, upon adjudication, be liable to a penalty up to thrice the sum involved in such contravention where such amount is quantifiable, or up to two lakh rupees where the amount is not quantifiable, and where such contrav ntion is a continying one, further penalty which may extend to five thousand rupees for every day after the first day during which the contravention continues.
• Any Adjudicating Authority adjudging any contravention under sub-section (1), may, if he thinks fit in addition to any penalty which he may impose for such contravention direct that any currency, security or any other money or property in respect of hich the contravention has taken place shall be confiscated to the Central Government and further direct that the foreign exchange holdings, if any, of the persons committing the contraventions or any part thereof, shall be brought back into India or sha l be retained outside India in accordance with the directions made in this behalf. Explanation.-For the purposes of this sub-section, "property" in respect of which contravention has taken place, shall includeo
deposits in a bank, where the said property is converted into such deposits;
o Indian currency, where the said property is converted into that currency; and
o any other property which has resulted out of the conversion of that property.
Enforcement of te orders of Adjudicating Authority.
• Subject to the provisions of sub-section (2) of section 19, if any person fails to make full payment of the penalty imposed on him under section 13 within a period of ninety days from the date n which the notice for payment of such penalty is served on him, he shall be liable to civil imprisonment under this section.
• No order for the arrest and detention in civil prison of a defaulter shall be made unless the Adjudication Authority has issued and served a notice upon the defaulter calling upon him to appear before him on the date specified in the notice and to sh w cause why he should not be committed to the civil prison,

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and unless the Adjudicating Authority, for reasons in writing, is satisfiedo
that the defaulter, with the object or effect of obstructing the recovery
of penalty, has after the issue of notice by the Adjudicating Authority,
dishonestly transferred, concealed, or removed any part of his property,
or
o that the defaulter has, or has had since the issuing of notice by the
Adjudicating Authority, the means to pay the arrears or some
substantial part thereof and refuses or neglects or has refused or
neglected to pay the same.
• Notwithstanding anything contained in sub-section (1), a warrant for the arrest
of the defaulter may be issued by the Adjudicating Authority if the
Adjudicating Authority is satisfied, by affidavit or otherwise, that with the
object or effect of dela ing the execution of the certificate the defaulter is
likely to abscond or leave the local limits of the jurisdiction of the
Adjudicating Authority.
• Where appearance is not made pursuant to a notice issued and served under
sub-section (1), the Adjudicating Authority may issue a warrant for the arrest
of the defaulter.
• A warrant of arrest issued by the Adjudicating Authority under sub-section (3)
or sub-section (4) may also be executed by any other Adjudicating Authority
within whose jurisdiction the defaulter may for the time being be found.
• Every person arrested in pursuance of a warrant of arrest under this section
shall be brought before the Adjudicating Authority issuing the warrant as soon
as practicable and in any event within twenty-four hours of his arrest
(exclusive of the time equired for the journey): Provided that, if the defaulter
pays the amount entered in the warrant of arrest as due and the costs of the
arrest to the officer arresting him, such officer shall at once release him.
Explanation.-For the purposes of this sub-section, where the defaulter is a
Hindu undivided family, the karta thereof shall be deemed to be the defaulter.
• When a defaulter appears before the Adjudicating Authority pursuant to a
notice to show cause or is brought before the Adjudicating Authority under
this section, the Adjudicating Authority shall give the defaulter an opportunity
showing cause why he hould not be committed to the civil prison.
• Pending the conclusion of the inquiry, the Adjudicating Authority may, in his
discretion, order the defaulter to be detained in the custody of such officer as
the Adjudicating Authority may think fit or release him on his furnishing the
security to t e satisfaction of the Adjudicating Authority for his appearance as
and when required.
• Upon the conclusion of the inquiry, the Adjudicating authority may make an
order for the detention of the defaulter in the civil prison and shall in that
event cause him to be arrested if he is not already under arrest: Provide that in
order to give a defaulter an opportunity of satisfying the arrears, the
Adjudicating Authority may, before making the order of detention, leave the
defaulter in the custody of the officer arresting him or of any other officer for
a specif ed period not exceeding fifteen days, or release him on his furnishing
security to the satisfaction of the Adjudicating Authority for his appearance at
the expiration of the specified period if the arrears are not satisfied.
• When the Adjudicating Authority does not make an order of detention under
sub-section (9), he shall, if the defaulter is under arrest, direct his release.
• Every person detained in the civil prison in execution of the certificate may be
so detained,-
o where the certificate is for a demand of an amount exceeding rupees
one crore, up to three years, and
o in any other case, up to six months: Provided that he shall be released
from such detention on the amount mentioned in the warrant for his
detention being paid to the officer-in-charge of the civil prison.
• A defaulter released from detention under this section shall not, merely by
reason of his release, be discharged from his liability for the arrears, but he
shall not be liable to be arrested under the certificate in execution of which he
was detaine in the civil prison.
• A detention order may be executed at any place in India in the manner
provided for the execution of warrant of arrest under the Code of Criminal
Procedure, 1973 (2 of 1974).
Power to compound contravention.
• Any contravention under section 13 may, on an application made by the
person committing such contravention, be compounded within one hundred
and eighty days from the date of receipt of application by the Director f
Enforcement or such other officers of the Directorate of Enforcement and
officers of the Reserve Bank as may be authorised in this behalf by the Central
Government in such manner as may be prescribed.
• Where a contravention has been compounded under sub-section (1), no
proceeding or further proceeding, as the case may be, shall be initiated or
continued, as the case may be, against the person committing such
contravention under that section, in re pect of the contravention so
compounded.

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ADJUDICATION AND APPEAL

CHAPTER V- ADJUDICATION AND APPEAL

Appointment of Adjudicating Authority.

• For the purpose of adjudication under section 13, the Central Government may, by an order published in the Official Gazette, appoint as many officers of the Central Government as it may think fit, as the Adj dicating Authorities for holding an inquiry in the manner prescribed after giving the person alleged to have committed contravention under section 13, against whom a complaint has been made under sub-section (3) (hereinafter in this section referred to a the said person) a reasonable opportunity of being heard for the purpose of imposing any penalty: Provided that where the Adjudicating Authority is of opinion that the said person is likely to abscond or is likely to evade in any manner, the payment of penalty, if levied, it may direct the said person to furnish a bond or guarantee for such amount an subject to such conditions as it may deem fit.

• The Central Government shall, while appointing the Adjudicating Authorities under sub-section (1), also specify in the order published in the Official Gazette, their respective jurisdictions.

• No Adjudicating Authority shall hold an enquiry under sub-section (1) except upon a complaint in writing made by any officer authorised by a general or special order by the Central Government.

• The said person may appear either in person or take the assistance of a legal practitioner or a chartered accountant of his choice for presenting his case before the Adjudicating Authority.

• Every Adjudicating Authority shall have the same powers of a civil court which are conferred on the Appellate Tribunal under sub-section (2) of section 28 ando

all proceedings before it shall be deemed to be judicial proceedings within the meaning of sections 193 and 228 of the Indian Penal Code (45 of 1860);

o shall be deemed to be a civil court for the purposes of sections 345 and 346 of the Code of Criminal Procedure, 1973 (2 of 1974).

• Every Adjudicating Authority shall deal with the complaint under sub-section (2) as expeditiously as possible and endeavor shall be made to dispose of the complaint finally within one year from the date of receipt of the complaint: Provided that where the complaint cannot be disposed of within the said period, the Adjudicating Authority shall record periodically the reasons in writing for not disposing of the complaint within the said period.

Appeal to Special Director (Appeals).

• The Central Government shall, by notification, appoint one or more Special Directors (Appeals) to hear appeals against the orders of the Adjudicating Authorities under this section and shall also specify in t e said notification the matter and places in relation to which the Special Director (Appeals) may exercise jurisdiction.

• Any person aggrieved by an order made by the Adjudicating Authority, being an Assistant Director of Enforcement or a Deputy Director of Enforcement, may prefer an appeal to the Special Director (Appeals).

• Every appeal under sub-section (1) shall be filed within forty-five days from the date on which the copy of the order made by the Adjudicating Authority is received by the aggrieved person and it shall be in such form, verified in such manner and be ccompanied by such fee as may be prescribed: Provided that the Special Director (Appeals) may entertain an appeal after the expiry of the said period of forty-five days, if he is satisfied that there was sufficient cause for not filing it within that period.

• On receipt of an appeal under sub-section (1), the Special Director (Appeals) may after giving the parties to the appeal an opportunity of being heard, pass such order thereon as he thinks fit, confirming, modifying or setting aside the order appeale against.

• The Special Director (Appeals) shall send a copy of every order made by him to the parties to appeal and to the concerned Adjudicating Authority.

• The Special Director (Appeals) shall have the same powers of a civil court which are conferred on the Appellate Tribunal under sub-section (2) of section 28 ando

all proceedings before him shall be deemed to be judicial proceedings within the meaning of sections 193 and 228 of the Indian Penal Code (45 of 1860);

o shall be deemed to be a civil court for the purposes of sections 345 and 346 of the Code of Criminal Procedure, 1973 (2 of 1974).

Establishment of Appellate Tribunal.
Establishment of Appellate Tribunal.-The Central Government shall, by notification, establish an Appellate Tribunal to be known as the Appellate Tribunal for Foreign Exchange to hear appeals against the orders of the Adjudicating Authorities and the pecial Director (Appeals) under this Act.
Appeal to Appellate Tribunal.
• Save as provided in sub-section (2), the Central Government or any person aggrieved by an order made by an Adjudicating Authority, other than those referred to in sub-section (1) of section 17, or the Special Directo (Appeals), may prefer an appeal to the Appellate Tribunal: Provided that any person appealing against the order of the Adjudicating Authority or the Special Director (Appeals) levying any penalty, shall while filing the appeal, deposit the amount of such penalty with such authority as may be notified by the Cent al Government:
Provided further that where in any particular case, the Appellate Tribunal is of the opinion that the deposit of such penalty would cause undue hardship to such person, the Appellate Tribunal may dispense with such deposit subject to such conditions as i may deem fit to impose so as to safeguard the realisation of penalty.
• Every appeal under sub-section (1) shall be filed within a period of forty-five days from the date on which a copy of the order made by the Adjudicating Authority or the Special Director (Appeals) is received by the aggrieved person or by the Central Government and it shall be in such form, verified in such manner and be accompanied by such fee as may be prescribed : Provided that the Appellate Tribunal may entertain an appeal after the expiry of the said period of forty-five days if it is satisfied that there was sufficient cause for not filing it within that period.
• On receipt of an appeal under sub-section (1), the Appellate Tribunal may, after giving the parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit, confirming, modifying or setting aside the order appealed agai st.
• The Appellate Tribunal shall send a copy of every order made by it to the parties to the appeal and to the concerned Adjudicating Authority or the Special Director (Appeals), as the case may be.
• The appeal filed before the Appellate Tribunal under sub-section (1) shall be dealt with by it as expeditiously as possible and endeavour shall be made by it to dispose of the appeal finally within one hundred and eighty days from the date of receipt of the appeal: Provided that where any appeal could not be disposed of within the said period of one hundred and eighty days, the Appellate Tribunal shall record its reasons in writing for not disposing off the appeal within the said period.
• The Appellate Tribunal may, for the purpose of examining the legality, propriety or correctness of any order made by the Adjudicating Authority under section 16 in relation to any proceeding, on its own motion or otherwise, call for the records of su h proceedings and make such order in the case as it thinks fit.
Composition of Appellate Tribunal.
• The Appellate Tribunal shall consist of a Chairperson and such number of Members as the Central Government may deem fit.
• Subject to the provisions of this Act,-]
o the jurisdiction of the Appellate Tribunal may be exercised by Benches thereof;
o a Bench may be constituted by the Chairperson with one or more Members as the Chairperson may deem fit;
o the Benches of the Appellate Tribunal shall ordinarily sit at New Delhi and at such other places as the Central Government may, in consultation with the Chairperson, notify;
o the Central Government shall notify the areas in relation to which each Bench of the Appellate Tribunal may exercise jurisdiction
• Notwithstanding anything contained in sub-section (2), the Chairperson may transfer a Member from one Bench to another Bench.
• If at any stage of the hearing of any case or matter it appears to the Chairperson or a Member that the case or matter is of such a nature that it ought to be heard by a Bench consisting of two Members, the case or matter may be transferred by the Ch irperson or, as the case may be, referred to him for transfer, to such Bench as the Chairperson may deem fit.
Qualifications for appointment of Chairperson, Member andSpecial Director (Appeals).
• A person shall not be qualified for appointment as the Chairperson or a Member unless heo
in the case of Chairperson, is or has been, or is qualified to be, a Judge of a High Court; and
o in the case of a Member, is or has been, or is qualified to be, a District Judge.
• A person shall not be qualified for appointment as a Special Director

(Appeals) unless heo
has been a member of the Indian Legal Service and has held a post in
Grade I of that Service; or
o has been a member of the Indian Revenue Service and has held a post
equivalent to a Joint Secretary to the Government of India.
Term of Office.
The Chairperson and every other Member shall hold office as such for a term of five
years from the date on which he enters upon his office: Provided that no Chairperson
or other Member shall hold office as such after he has attained,-
• in the case of the Chairperson, the age of sixty-five years;
• in the case of any other Member, the age of sixty-two years.
Term and Conditions of service.
The salary and allowances payable to and the other terms and conditions of service of
the Chairperson, other Members and the Special Director (Appeals) shall be such as
may be prescribed:
Provided that neither the salary and allowances nor the other terms and conditions of
service of the Chairperson or a Member shall be varied to his disadvantage after
appointment.
Vacancies.
-If, for reason other than temporary absence, any vacancy occurs in the office of the
Chairperson or a Member, the Central Government shall appoint another person in
accordance with the provisions of this Act to fill the vacancy and the pro eedings may
be continued before the Appellate Tribunal from the stage at which the vacancy is
filled.
Resignation and removal.
• The Chairperson or a Member may, by notice in writing under his hand
addressed to the Central Government, resign his office:Provided that the
Chairperson or a Member shall, unless he is permitted by the Central
Government to relinquish his office sooner, continue to hold office until the
expiry of three months from the date of receipt of such notice or until a person
duly app inted as his successor enters upon his office or until the expiry of
term of office, whichever is the earliest.
• The Chairperson or a Member shall not be removed from his office except by
an order by the Central Government on the ground of proved misbehaviour or
incapacity after an inquiry made by such person as the President may appoint
for this purpose in whi h the Chairperson or a Member concerned has been
informed of the charges against him and given a reasonable opportunity of
being heard in respect of such charges.
Member to act as Chairperson in certain circumstances.
• In the event of the occurrence of any vacancy in the office of the Chairperson
by reason of his death, resignation or otherwise, the senior-most Member shall
act as the Chairperson until the ate on which a new Chairperson, appointed in
accordance with the provisions of this Act to fill such vacancy, enters upon his
office.
• When the Chairperson is unable to discharge his functions owing to absence,
illness or any other cause, the senior-most Member shall discharge the
functions of the Chairperson until the date on which the Chairperson resumes
his duties.
Staff of Appellate Tribunal and Special Director (Appeals).
• The Central Government shall provide the Appellate Tribunal and the Special
Director (Appeals) with such officers and employees as it may deem fit.
• The officers and employees of the Appellate Tribunal and office of the Special
Director (Appeals) shall discharge their functions under the general
superintendence of the Chairperson and the Special Director (Appeals), as the
case may be.
• The salaries and allowances and other conditions of service of the officers and
employees of the Appellate Tribunal and office of the Special Director
(Appeals) shall be such as may be prescribed.
Procedure and powers of Appellate Tribunal and Special Director(Appeals).
• The Appellate Tribunal and the Special Director (Appeals) shall not be bound
by the procedure laid down by the Code of Civil Procedure, 1908 (5 of 1908),
but shall be guid d by the principles of natural justice and, subject to the other
provisions of this Act, the Appellate Tribunal and the Special Director
(Appeals) shall have powers to regulate its own procedure.
• The Appellate Tribunal and the Special Director (Appeals) shall have, for the
purposes of discharging its functions under this Act, the same powers as are
vested in a civil court under the Code of Civil Procedure, 1908 (5 of 1908)
while trying a suit in respect of the following matters, namely:-
o summoning and enforcing the attendance of any person and examining
him on oath;
o requiring the discovery and production of documents;
o receiving evidence on affidavits;
o subject to the provisions of sections 123 and 124 of the Indian
Evidence Act, 1872 (1 of 1872), requisitioning any public record or
document or copy of such record or document from any office;

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o issuing commissions for the examination of witnesses or documents;
o reviewing its decisions;
o dismissing a representation of default or deciding it ex parte;
o setting aside any order of dismissal of any representation for default or any order passed by it ex parte; and
o any other matter which may be prescribed by the Central Government.
• An order made by the Appellate Tribunal or the Special Director (Appeals) under this Act shall be executable by the Appellate Tribunal or the Special Director (Appeals) as a decree of civil court and, for this purpose, the Appellate Tribunal and the pecial Director (Appeals) shall have all the powers of a civil court.
• Notwithstanding anything contained in sub-section (3), the Appellate Tribunal or the Special Director (Appeals) may transmit any order made by it to a civil court having local jurisdiction and such civil court shall execute the order as if it were a ecree made by that court.
• All proceedings before the Appellate Tribunal and the Special Director (Appeals) shall be deemed to be judicial proceedings within the meaning of sections 193 and 228 of the Indian Penal Code (45 of 1860) and the Appellate Tribunal shall be deemed to be a civil court for the purposes of sections 345 and 346 of the Code of Criminal Procedure, 1973 (2 of 1974).
Distribution of business amongst Benches.
Distribution of business amongst Benches.-Where Benches are constituted, the Chairperson may, from time to time, by notification, make provisions as to the distribution of the business of the Appellate Tribunal amongst the Benches and also provide fo the matters which may be dealt with by each Bench.
Power of Chairperson to transfer cases.
Power of Chairperson to transfer cases.-On the application of any of the parties and after notice to the parties, and after hearing such of them as he may desire to be heard, or on his own motion without such notice, the Chairperson may transfer any ase pending before one Bench, for disposal, to any other Bench.
Decision to be by majority.
Decision to be by majority.-If the Members of a Bench consisting of two Members differ in opinion on any point, they shall state the point or points on which they differ, and make a reference to the Chairperson who shall either hear the point or poi ts himself or refer the case for hearing on such point or points by one or more of the other Members of the Appellate Tribunal and such point or points shall be decided according to the opinion of the majority of the Members of the Appellate Tribunal who have heard the case, including those who first heard it.
Right of appellant to take assistance of legal practitioner orchartered accountant and of Government, to appoint presentingofficers.
Right of appellant to take assistance of legal practitioner or chartered accountant and of Government, to appoint presenting officers.-
• A person preferring an appeal to the Appellate Tribunal or the Special Director (Appeals) under this Act may ei her appear in person or take the assistance of a legal practitioner or a chartered accountant of his choice to present his case before the Appellate Tribunal or the Special Director (Appeals), as the case may be.
• The Central Government may authorise one or more legal practitioners or chartered accountants or any of its officers to act as presenting officers and every person so authorised may present the case with respect to any appeal before the Appellate Tri unal or the Special Director (Appeals), as the case may be.
Members, etc., to be public servants.
Members, etc., to be public servants.-The Chairperson, Members and other officers and employees of the Appellate Tribunal, the Special Director (Appeals) and the Ajudicating Authority shall be deemed to be public servants within the meaning of secti n 21 of the Indian Penal Code (45 of 1860).
Civil court not to have jurisdiction.
Civil court not to have jurisdiction.-No civil court shall have jurisdiction to entertain any suit or proceeding in respect of any matter which an Adjudicating Authority or the Appellate der this Act to determine and no injunction shall be granted by any court or other authority in respect of any action taken or to be taken in pursuance of any power conferred by or under this Act. Tribunal or the Special Director (Appeals) is empowered by or u
Appeal to High Court.
Appeal to High Court.-Any person aggrieved by any decision or order of the Appellate Tribunal may file an appeal to the High Court within sixty days from the date of communication of the decision or order of the Appellate Tribunal to him on any quest on of law arising out of such order:
Provided that the High Court may, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period not exceeding sixty days.
Explanation.-In this section "High Court" means-
• the High Court within the jurisdiction of which the aggrieved party ordinarily resides or carries on business or personally works for gain; and

• where the Central Government is the aggrieved party, the High Court within the jurisdiction of which the respondent, or in a case where there are more than one respondent, any of the respondents, ordinarily resides or carries on business or personall works for gain.

DIRECTORATE OF ENFORCEMENT

CHAPTER VI-DIRECTORATE OF ENFORCMENT

Directorate of Enforcement.

• The Central Government shall establish a Directorate of Enforcement with a Director and such other officers or class of officers as it thinks fit, who shall be called officers of Enforcement, for the purposes of this A t.
• Without prejudice to the provisions of sub-section (1), the Central Government may authorise the Director of Enforcement or an Additional Director of Enforcement or a Special Director of Enforcement or a Deputy Director of Enforcement to appoint offi ers of Enforcement below the rank of an Assistant Director of Enforcement.
• Subject to such conditions and limitations as the Central Government may impose, an officer of Enforcement may exercise the powers and discharge the duties conferred or imposed on him under this Act.
Power of search, seizure, etc.
• The Director of Enforcement and other officers of Enforcement, not below the rank of an Assistant Director, shall take up for investigation the contravention referred to in section 13.
• Without prejudice to the provisions of sub-section (1), the Central Government may also, by notification, authorise any officer or class of officers in the Central Government, State Government or the Reserve Bank, not below the rank of an Under Secre ary to the Government of India to investigate any contravention referred to in section 13.
• The officers referred to in sub-section (1) shall exercise the like powers which are conferred on income-tax authorities under the Income-tax Act, 1961 (43 of 1961) and shall exercise such powers, subject to such limitations laid down under that A t.
Empowering other officers.
• The Central Government may, by order and subject to such conditions and limitations as it thinks fit to impose, authorise any officer of customs or any central excise officer or any police officer or any other officer o the Central Government or a State Government to exercise such of the powers and discharge such of the duties of the Director of Enforcement or any other officer of Enforcement under this Act as may be stated in the order.
• The officers referred to in sub-section (1) shall exercise the like powers which are conferred on the income-tax authorities under the Income-tax Act, 1961 (43 of 1961), subject to such conditions and limitations as the Central Government may impose.

MISCELLANEOUS
CHAPTER VII-MISCELLANEOUS

Presumption as to documents in certain cases.
Presumption as to documents in certain cases.-Where any document-
• is produced or furnished by any person or has been seized from the custody or control of any person, in either case, under this Act or under any other law; or
• has been received from any place outside India (duly authenticated by such authority or person and in such manner as may be prescribed) in the course of investigation of any contravention under this Act alleged to have been committed by any person, and such document is tendered in any proceeding under this Act in evidence against him, or against him and any other person who is proceeded against jointly with him, the court or the Adjudicating Authority, as the case may be, shallo
presume, unless the contrary is proved, that the signature and every other part of such document which purports to be in the handwriting of any particular person or which the court may reasonably assume to have been signed by, or to be in the handwri ing of, any particular person, is in that person's handwriting, and in the case of a document executed or attested, that it was executed or attested by the person by

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whom it purports to have been so executed or attested;
o admit the document in evidence notwithstanding that it is not duly stamped, if such document is otherwise admissible in evidence;
o in a case falling under clause (i), also presume, unless the contrary is proved, the truth of the contents of such document.
Suspension of operation of this Act.
• If the Central Government is satisfied that circumstances have arisen rendering it necessary that any permission granted or restriction imposed by this Act should cease to be granted or imposed, or if it consi ers necessary or expedient so to do in public interest, the Central Government may, by notification, suspend or relax to such extent either indefinitely or for such period as may be notified, the operation of all or any of the provisions of this Act.
• Where the operation of any provision of this Act has under sub-section (1) been suspended or relaxed indefinitely, such suspension or relaxation may, at any time while this Act remains in force, be removed by the Central Government by notification.
• Every notification issued under this section shall be laid, as soon as may be after it is issued, before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more succe sive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the notification or both Houses agree that the notification should not be issu d, the notification shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that not fication.
Power of Central Government to give directions.
Power of Central Government to give directions.-For the purposes of this Act, the Central Government may, from time to time, give to the Reserve Bank such general or special directions as it thinks fit, and the Reserve Bank shall, in the discharge of its functions under this Act, comply with any such directions.
Contravention by companies.
• Where a person committing a contravention of any of the provisions of this Act or of any rule, direction or order made thereunder is a company, every person who, at the time the contravention was committed, was in char e of, and was responsible to, the company for the conduct of the business of the company as well as the company, shall be deemed to be guilty of the contravention and shall be liable to be proceeded against and punished accordingly: Provided that nothing contained in this sub-section shall render any such person liable to punishment if he proves that the contravention took place without his knowledge or that he exercised due diligence to prevent such contravention.
• Notwithstanding anything contained in sub-section (1), where a contravention of any of the provisions of this Act or of any rule, direction or order made thereunder has been committed by a company and it is proved that the contravention has taken pla e with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of the contraven ion and shall be liable to be proceeded against and punished accordingly.Explanation.-For the purposes of this section-(i) "company" means any body corporate and includes a firm or other association of individuals; and
(ii) "director", in relation to a firm, means a partner in the firm.
Death or insolvency in certain cases.
Death or insolvency in certain cases.-Any right, obligation, liability, proceeding or appeal arising in relation to the provisions of section 13 shall not abate by reason of death or insolvency of the person liable under that section and upon such de th or insolvency such rights and obligations shall devolve on the legal representative of such person or the official receiver or the official assignee, as the case may be: Provided that a legal representative of the deceased shall be liable only to the extent of the inheritance or estate of the deceased.
Bar of legal proceedings.
Bar of legal proceedings.-No suit, prosecution or other legal proceeding shall lie against the Central Government or the Reserve Bank or any officer of that Government or of the Reserve Bank or any other person exercising any power or discharging any functions or performing any duties under this Act, for anything in good faith done or intended to be done under this Act or any rule, regulation, notification, direction or order made thereunder.
Removal of difficulties.
• If any difficulty arises in giving effect to the provisions of this Act, the Central Government may, by order, do anything not inconsistent with the provisions of this Act for the purpose of removing the difficulty: Provided that no such order shall be made under this section after the expiry of two years from the commencement of this Act.
• Every order made under this section shall be laid, as soon as may be after it is

made, before each House of Parliament.
Power to make rules.
The Central Government may, by notification, make rules to carry out the provisions of this Act. (2) Without prejudice to the generality of the foregoing power, such rules may provide for,-
• the imposition of reasonable restrictions on current account transactions under section 5;
• the manner in which the contravention may be compounded under sub-section (1) of section 15;
• the manner of holding an inquiry by the Adjudicating Authority under subsection (1) of section 16;
• the form of appeal and fee for filing such appeal under sections 17 and 19;
• the salary and allowances payable to and the other terms and conditions of service of the Chairperson and other Members of the Appellate Tribunal and the Special Director (Appeals) under section 23;
• the salaries and allowances and other conditions of service of the officers and employees of the Appellate Tribunal and the office of the Special Director (Appeals) under sub-section (3) of section 27;
• the additional matters in respect of which the Appellate Tribunal and the Special Director (Appeals) may exercise the powers of a civil court under clause (i) of sub-section (2) of section 28;
• the authority or person and the manner in which any document may be authenticated under clause (ii) of section 39; and
• any other matter which is required to be, or may be, prescribed.
Power to make regulations.
• The Reserve Bank may, by notification, make regulations to carry out the provisions of this Act and the rules made thereunder.
• Without prejudice to the generality of the foregoing power, such regulations may provide for,-
o the permissible classes of capital account transactions, the limits of admissibility of foreign exchange for such transactions, and the prohibition, restriction or regulation of certain capital account transactions under section 6;
o the manner and the form in which the declaration is to be furnished under clause (a) of sub-section (1) of section 7;
o the period within which and the manner of repatriation of foreign exchange under section 8;
o the limit up to which any person may possess foreign currency or foreign coins under clause (a) of section 9;
o the class of persons and the limit up to which foreign currency account may be held or operated under clause (b) of section 9;
o the limit up to which foreign exchange acquired may be exempted under clause (d) of section 9;
o the limit up to which foreign exchange acquired may be retained under clause (e) of section 9;
o any other matter which is required to be, or may be, specified.
Rules and regualations to be laid before Parliament.
Every rule and regulation made under this Act shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session for a total period of thirty days which may b comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the rule or regulation, or b th Houses agree that the rule or regulation should not be made, the rule or regulation shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without p ejudice to the validity of anything previously done under that rule or regulation.
Repeal and saving.
• The Foreign Exchange Regulation Act, 1973 (46 of 1973) is hereby repealed and the Appellate Board constituted under sub-section (1) of section 52 of the said Act (hereinafter referred to as the repealed Act) shall stand dissolv d.
• On the dissolution of the said Appellate Board, the person appointed as Chairman of the Appellate Board and every other person appointed as Member and holding office as such immediately before such date shall vacate their respective offices and no su h Chairman or other person shall be entitled to claim any compensation for the premature termination of the term of his office or of any contract of service.
• Notwithstanding anything contained in any other law for the time being in force, no court shall take cognizance of an offence under the repealed Act and no adjudicating officer shall take notice of any contravention under section 51 of the repealed A t after the expiry of a period of two years from the date of the commencement of this Act.
• Subject to the provisions of sub-section (3) all offences committed under the repealed Act shall continue to be governed by the provisions of the repealed Act as if that Act had not been repealed.

• Notwithstanding such repeal,-
o anything done or any action taken or purported to have been done or taken including any rule, notification, inspection, order or notice made or issued or any appointment, confirmation or declaration made or any licence, permission, authorization or e emption granted or any document or instrument executed or any direction given under the Act hereby repealed shall, in so far as it is not inconsistent with the provisions of this Act, be deemed to have been done or taken under the corresponding provision of this Act;
o any appeal preferred to the Appellate Board under sub-section (2) of section 52 of the repealed Act but not disposed of before the commencement of this Act shall stand transferred to and shall be disposed of by the Appellate Tribunal constituted unde this Act;
o every appeal from any decision or order of the Appellate Board under sub-section (3) or sub-section (4) of section 52 of the repealed Act shall, if not filed before the commencement of this Act, be filed before the High Court within a period of sixty days of such commencement :Provided that the High Court may entertain such appeal after the expiry of the said period of sixty days if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within the said period.
• Save as otherwise provided in sub-section (3), the mention of particular matters in sub-sections (2), (4) and (5) shall not be held to prejudice or affect the general application of section 6 of the General Clauses Act, 1897 (10 of 1897) with regard to the effect of repeal.

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Foreign Exchange

Foreign Exchange
It includes all Currency, deposits, Credits and Balances payable in Foreign currency. It also includes Drafts/TCs, LCs and Bills of Exchange payable in Foreign currency. In nut shell, all claims payable abroad is Foreign Exchange.
On the other hand, Foreign Currency is narrow term which includes hard currency say Pounds, Dollars etc.

Forex Market It comprises of individuals and entities including banks across the globe without geographical boundaries. Forex market is dynamic and it operates round the clock. Exchange rate of major currencies change after about **every 4 seconds.** It opens from **Monday to Friday** except in Middle east countries where it is closed on Friday and opens on Saturday and Sunday.

Exchange Rate mechanism

When settlement of funds and exchange of currency takes place__________
TOD rate or Cash Rate Same day (it is also called ready rate)
TOM Rate Next working day
Spot Rate 2nd working day (48 hours)
Forward Rate After few days/months
If Next day or 2nd day is holiday in either of the two countries, the settlement will take place on next day. For example Spot deal is stuck on 23rd Dec. 25th is Christmas Day and 26th is Sunday. Under such circumstances, value date will be 27th i.e. Monday.
There are two types of rates- Fixed and Floating. Floating rates are determined by market forces of Demand and Supply. India switched to Floating exchange rates regime in 1993.
Buy and Sell
Maxim
Buy Low Sell High (Direct Quotations)
Buy rate is also called **Bid Rate** and Sell Rate is called **Offer Rate.**
Buy High Sell Low (Indirect Quotations)
When Local Currency is fixed, bank will like to have more foreign

currency while buying and give less foreign currency while selling**.**

Forward Rates

(Premium is
always added and
Discount is
always deducted
from Spot Rate to
arrive at Forward
Rate)

It is required when currency is exchanged after few months/days.

Buy Transactions :

Spot Rate (+) premium OR (-) Discount

(Lower premium is added OR Higher discount is deducted)

Sale Transactions:

Spot Rate (+)Higher premium OR (-) Lower discount

(So that currency may become cheaper while buying and dearer while
selling

In India, Forward Contracts are available for Maximum period
of 12 Months

EXCHANGE CONTROL REGULATIONS

Exchange control was first introduced in India on Sept 3, 1939. Subsequently it was brought under Foreign Exchange Regulation Act, 1973. At present it is regulated through FEMA 1999.

The objectives of ECR are

a conservation of foreign exchange;

b proper accounting of foreign exchange receipts and payments;

c stabilizing the external value of the rupee;

d to prevent flight of scarce capital by control over remittances abroad and supervision of accounts of nonresidents, so that the balance of payments deficit does not occur or does'not worsen;

e to check smuggling;

f to fulfil IMF obligations .

LIBERALISED REMITTANCE SCHEME (LRS) FOR RESIDENT INDIVIDUALS

RBI introduced LRS on Feb 04, 2004. Major changes were made by RBI in LRS w.e.f. 01.06.2015 (based on Govt. notification 15.05.15).

Eligibility: All resident individuals including minors and non-individuals are eligible.

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

It is mandatory to have PAN number to make remittances.

Forex can be purchased from authorised person which indude AD Category-1 Banks, AD Category-2 and Full Fledged Money Changers.

Capital Accounts transactions Remittances up to USD 250,000 per financial year can be allowed for permissible capital account transactions as under: I) opening of foreign currency account abroad; ii) purchase of property abroad;

ill) making investments abroad;

iv) setting up Wholly owned subsidiaries and Joint Ventures abroad;

v) loans including in Indian Rupees to Non-resident Indians relatives as defined in Companies Act, 2013.

Current account transactions • : All facilities (Including private/business visits) for remittances have been subsumed under overall limit of USD 250,000/FY.

Facilities for Individuals

1. Individuals can avail of forex facility for the following purposes within the limit of USD 250000. Additional remittance shall require prior approval of RBI.

1. Private visits to a country (except Nepal & Bhutan)

2. Gift or donation.

3. Going abroad for employment or immigration.

4. Maintenance of close relatives abroad

5. Travel for business, or attending a conference or specialized training or for meeting medical expenses, or check-up abroad, or for accompanying as attendant to a patient going abroad for medical treatment/ check-up.

7. Expenses for medical treatment abroad

B. Studies abroad

9. Any other current account transaction

Exception : For immigration,medical treatment and studies abroad, the individualmay avail of exchange facility in excess of LRS limit if required by a country of emigration,medical institute offering treatment or the university, respectively.

Facilities for persons other than individual The following remittances shall require RBI approval:

(i) Donations beyond 1%of forex earnings in previous 3 FY or USD 5000000, whichever is less, for:

a) creation of Chairs in reputed educational institutes,

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b) contribution to funds (not being an investment fund) promoted by educational institutes; and
c) technical institution/body/ 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 5%of inward remittance whichever ismore.
(iii) Remittances exceeding USD 10000000 per project for any consultancy services for infrastructure projects and USD 1,000,000 per project, for other consultancy services procured fromoutside India.
(iv) Remittances exceeding 5%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.

Mode of remittance: The Scheme can be used for outward remittance in the formof 'a DD either in the resident individual's own name or in the name of beneficiary with whomhe intends putting through the permissible transactions at the time of private visit abroad, can be effected, against self declaration of the remitter in the format prescribed.
Loan facility : Banks **should not extend** any kind of credit facilities to resident individuals to facilitate remittances under the Scheme.
Remittances not available under the scheme:
i. Remittance for any purpose specifically prohibited under Schedule-I (like purchase of lottery/sweep stakes, tickets, prescribedmagazines etc.) or itemrestricted under Schedule II of FEMA (Current A/c Transactions) Rules, 2000.
ii. Remittancesmade to Bhutan,Nepal,Mauritius or Pakistan.
iii. Remittancesmade to countries identified by the Financial Action Task Force (FATF) as "non co-operative countries and territories" as available on FATF website (viz Cook Islands, Egypt, Guatemala, Indonesia, Myanmar, Nauru, Nigeria, Philippines and Ukraine) or as notified by RBI.
iv. Remittances to individuals and entities identified as posing significant risk of committing acts of terrorismas advised separately by RBI to the banks.

Reporting of the transactions: The remittancesmade will be reported in the R-Return in the normal course. The ADsmay also prepare and keep on record dummy FormA2, in respect of remittances exceeding USD 5000.
With effect from01.07.13, the banks are required to upload the data inOnline Return Filing System(OAFS) on a monthly basis, by 5th of the followingmonth to which it relates.Where there is no information, 'nil' figure is to be uploaded.

Rules related to release / remittance of foreign exchange to residents
ADbanks can release forex to residents in India as per Rules framed u/s Sec 5 of FEMA. Forex cannot be released for Schedule I transactions. For Schedule II transactions,Govt. permission is required. For Schedule III transactions, forex can be released up to specified limit byADbanks. Beyond that limit, approval of RBI is required.
Ceilings on release of amount by ADs without RBI approval are given above, under LRS.
Nepal & Bhutan - Forex for any kind of travel to or for any transactionwith persons resident inNepal andBhutan cannot be released. Any amount of Indian currency can be used.Highest denomination of currency note can beRs.100.
Up to Rs.25000, any denomination is allowed.
Form of foreign currency: 1. Coins, currency notes and traveller's cheques. Currency notes/coins can be up to US$ 3000. The balance can be traveller's cheque or banker's draft.
2. For Iraq and Libya currency notes and coins can be obtained up toUS$ 5000 or its equivalent.
3. For Iran, Russian Federation, and other Republics of Commonwealth of Independent Countries, no ceiling.
Mode of purchase: In cash up toRs.50,000/-.Above this, payment byway of a crossed cheque/banker's cheque/pay order/demand draft / debit card / credit card only.
Surrender of unused forex: Currency notes and travellers' cheques within 180 days of return.
Retention of unused forex : US$2,000 or its equivalent. There is no restriction on residents for holding foreign currency coins.

Use of International Credit Card (ICC): Use of the ICCs / ATMs/ Debit Cards can be made for personal payments and for travel abroad for various purposes, only up to specified limits.
Export / Import of Indian currency by Residents or non-residents : Up to Rs. 25000 each to or from any country other than Nepal or Bhutan (Pakistan & Bangladesh Rs.10000).
Import of Foreign exchange from abroad: Any amount subject to declaration on CDF.
Mandatory CDF : Where total amount exceeds US$ 10,000 (or its equivalent) and/or value of foreign currency notes exceeds US$ 5,000, declaration should be made to the Customs Authorities through Currency Declaration Form (CDF), on arrival in India.

Application for purchase of FC : Form A2. It is not required up to $ 25000. A2 to be preserved by banks for one year for verification by Auditors. endorsement on Passport : It is not mandatory for Authorised Dealers to endorse the amount of foreign exchange sold for travel abroad on the passport of the traveller. However, if requested by the traveller, AD may record under its stamp, date and signature, details of foreign exchange sold for travel

.
Inward Remittance
1. Any person foreigner or Indian coming to India can bring any amount of foreign exchange in India.
2. If foreign currency being brought ismore than US$ 5000 or foreign currency and traveler cheque ismore than US $ 10,000, then the person bringing forex shouldmake declaration before Customs on the Currency Declaration form. If it is not submitted to Customs, then it can be submitted to Authorised Dealer while surrendering foreign

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exchange.
3. Unspent Foreign exchange should be surrendered within 180 days of arrival in India whether it is foreign currency or foreign traveler cheque.
4. A resident individual can retain up to US $ 2000. There is no limit on coins.
5. Indian rupees can be brought up to Rs 25000.
6. Full fledgedMoney Changers (FFMCs) are permitted to encash foreign currency andmake cash payment only up to USD 3000 or its equivalent. Amount exceeding USD 3000 or its equivalent has to be paid by way of demand draft or bankers' cheque. RBI has allowed banks to credit proceeds of demand drafts / bankers' cheques issued against encashment of foreign currency to the NRE account of the NRI account holder where the instruments issued to the NRE account holder are supported by encashment certificate issued by AD Category—I / Category —II.
7. Exchange regulations are not applicable in case of remittance to or from Nepal and Bhutan. Therefore, forex can neither be taken to nor brought from Nepal and Bhutan. Indian rupees can be taken to Nepal and Bhutan in the denomination of Rs 100 or below.

Non Residents and their Accounts

Who is Resident Indian? Who is Non- Resident
A person who resides in India for more than 182 days during preceding financial year is Resident Indian. A person who is not resident is Non-Resident.
Who is NRI? A person who is citizen of India but resides outside India owing to:
Employment, Business, vocation-------indicating indefinite period of stay outside.
Work abroad on assignment with Foreign Govt., UNO, and IMF etc.
Deputation officially.
Study abroad.
PIO - Persons of Indian Origin
PIO is a person who is citizen of any other country, but he at any time:
Held Indian Passport
He or his grand-parents or grand grand parents were Indian citizens by virtue of constitution of India or under Indian Citizenship Act.
The person is spouse of Indian Citizen.

Resident: As per section 2(v) of the FEMA 1999, a person is called resident in India if he stays in India formore than 182 days during the preceding financial year except those who have gone out of India for taking up employment outside India or for carrying on a business or vocation 'outside India or for any other purpose indicating his intention to stay abroad for indefinite period.
Non Resident: Person resident outside Indiameans a person who is not resident in India.
NRI has been defined in Income Tax Act.
RBI definition of NRI: However, as per RBI guidelines, a non resident Indian can be a person of Indian Nationality or a person of Indian Origin.
Person of Indian Nationality (PIN): A Person of Indian Nationality is one who holds an Indian passport at the time of opening the account.
Person of IndianOrigin: A Person of IndianOrigin is one who is presently not a national of Pakistan or Bangladesh and : (a) who at anytime held an Indian passport; or (b) he himself, either-of his parents or any of his grand parents was a citizen of India by virtue of Constitution of India or the Citizenship Act,1955 ; or (c) the person is a spouse of Person of Indian Nationality / Origin.
Overseas Corporate Bodies are those in which at least 60% shareholding is of NRI. OCBs are not allowed to open NRI accounts.
Students who go abroad for studies have also been given the facility of opening NRI accounts.
Non resident accounts are of 3 types (a) Non Resident ordinary (b) Non Resident (External) (c) Foreign Currency Non Resident (Bank) account. Salient features of these accounts are as under

Non Resident Ordinary account:
1. Type of account: Saving, Current, FD and RD
2. Credit: can be local income as well as remittance from abroad.
3. Currency of deposit Indian Rupees
4. Period of Deposit and interest rate : Fixed deposit can be opened for 7 days to 10 years and interest rate as applicable to domestic deposits
5. Joint account allowed with residents as well non residents (NRO is the only account which can be opened jointly with residents)
6. Interest income is taxable and tax will be deducted at source irrespective of type of account and amount of interest. The rate of tax on interest on deposits out of foreign remittance is 20%and on deposits from local income is 30%. Surcharge and education cess will be extra.
7. Power of Attorney is allowed to residents formaking local payments. Power of Attorney **can undertake** all focal payments in rupees including payments for eligible investments subject to compliance with relevant regulations

made by the Reserve Bank; and Remittance outside India of current income in India of the nonresident individual account holder, net of applicable taxes. The resident Power of Attorney holder is **not permitted** to repatriate outside India funds held in the account other than to the non-resident individual account holder nor tomake payment by way of gift to a resident on behalf of the non-resident account holder or transfer funds fromthe account to another NRO account.

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8. Repatriation is allowed as per following details: (i) Remittance outside India of current income like rent, dividend, pension, interest, etc. in India of the account holder. (ii) Remittance up to USD onemillion, per financial year (April-March), for all bonafide purposes, to the satisfaction of the authorised dealer bank. (iii) sale proceeds of immovable property up to US $ 10 lakh per financial year without waiting for 10 year period.

Non-Resident accounts can be opened:

- By any person resident outside India (other than a person resident in Nepal and Bhutan) can open NRO account, maintain it for 6M and can convert it into foreign currency after completion of stay provided no local funds are credited to the account.
- Deposit may be held jointly with residents
- Currency of Deposit is Indian Rupees
- Not Repatriable except for the following in the account - 1) Current income 2) Up-to USD 1 Million per financial year.
- Type of Deposit may be Savings, Current, Recurring, Fixed Deposit.
- Existing accounts of residents are converted to NRO category consequent upon their becoming NRIs.
- TDS called withholding Tax is applicable at 30% + Service Tax +Education Cess.
- Prior permission of RBI is required to open NRO account of Pakistani national. **However permission is not required**

Non Resident (External) and ForeignCurrencyNon Resident (Bank) account

There are certain common features in these accounts like

1. Credits: Only amount received from abroad can be credited to these accounts.
2. Joint account is allowed only with Non residents and not allowed with residents.
3. Power of attorney is allowed to residents. He can make local payments. POA can remit money abroad if permitted by Power of Attorney.
4. Maximum loan against NRE and FCNR(B) is allowed up to Rs 100 lakh.
5. Interest income is free of Income tax and therefore tax is not deducted at source
6. Repatriation: Entire balance including interest can be repatriated abroad.

The other features are:

- Deposits are held in Indian currency.
- The Principal and Interest both can be repatriated.
- Account holder bears the risk of fluctuations in currency rates.
- Account will be opened with proceeds from abroad.
- Funds originating in India cannot be deposited.
- Interest rates Have since been deregulated by RBI..
- No lien is permitted to be marked against SB deposits.

- **Joint account with Indians can be opened as Former or Survivor.**

- Cheque book and IBS allowed.
- Nomination in favor of NRI/Resident Indian allowed.
- Interest Income is exempt from Income Tax, Gift Tax or Wealth Tax.
- TOD allowed up to Rs. 50000/- for maximum 2 weeks.
- Account can be operated in India through mandate also.
- Loans against FDR to 3rd parties allowed provided NRI is personally present for documentation.

FCNR- B accounts

FCNRB accounts can also be opened by NRIs. The conditions of NRE deposits as explained above are also applicable on FCNR-B deposits with the following additional features:

- Only FD 1-5 years tenure can be opened.
- The amount is kept in Foreign Currency and repaid in the Foreign Currency.
- 6 currencies i.e. GBP, USD, Euro, JPY, CAD. AUD are eligible currencies for opening the account.
- No exchange risk for the customer. The bank bears the risk.
- Interest on the basis of 360 days in a year
- Half yearly intervals of 180 days
- Interest exemptions from I.T.
- Operating by P/A not permitted.
- The amount of Principle and Interest is freely repatriable
- Interest Rate on 1-3 years FD is **LIBOR + 200 bps** and that of 3-5 years FD is **LIBOR + 400 bps.**(Previously, it was LIBOR + 300 bps)

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Rupee Loans against NRE/FCNRB FDRs

Demand Loan or Overdraft is allowed against FDR. There is no maximum limitof loan against pledge of FDR (Which was**100 lac earlier)**. The loan can be availed for :
- Personal purpose.
- Investment.
- Purchase of property.

The loan can be repaid :
- From proceeds of abroad
- From NRE/FCNR account
- From local resources through NRO account.

Resident Accounts Operation Either or Survivor with non- resident

It has been decided that AD banks may include an NRI close relative (relatives as defined in Section 6 of the Companies Act, 1956) in existing / new resident bank accounts as joint holder with the resident account holder on **"Either or Survivor**" basis subject to the following conditions:

- Such account will be treated as resident bank account
- Cheques, instruments, remittances, cash, card belonging to the NRI close relative shall not be eligible for credit to this account
- The NRI close relative shall operate such account only for and on behalf of the resident for domestic payment

Where due to any eventuality, the non-resident account holder becomes the survivor, it shall be categorized as NRO account

Investments by NRIs in India

NRIs are allowed to invest in India on Repatriation basis as well as on Non-Repatriation basis. NRI can purchase Equity Shares, Preference shares and Convertible Debentures in Indian companies subject to conditions under following categories:
1. Foreign Direct Investments.
2. Portfolio Investment
3. Purchase and Sale of Shares on Non-Repatriation basis.
4. Purchase of other securities of Indian Companies.
5. Exchange Traded Derivatives.

Besides above, NRIs are permitted to invest in:
- Units of UTI and Mutual Funds
- Company Deposits – Minimum 3 years" period.
- Share in Proprietorship firm/partnership firm provided the firm is not engaged in Agriculture and Plantation activity or Property business.
- Acquiring of Immovable property not being Agriculture, Plantation or Farm House.

NRI can acquire IP by way of :
- Purchase out of funds received in India
- By way of gift from resident in India or outside India.
- By way of Inheritance from a person resident outside India.

The Income from the property or sale proceeds of the property can be repatriated outside India up to monetary limit of USD1 Million per financial year provided all the applicable taxes are paid.

NRIs can invest in Govt. securities, treasury bills on non- repatriation basis. However, NRI cannot invest in Small saving Schemes including PPF.

Loans to NRIs NRI can avail the following loans:

1. Rupee Loans in India
- Up to up to any limit subject to prescribed margin.
- For personal purpose, contribution to Capital in Indian Companies or for acquisition of property.
- Repayment of loan will be either from inward remittances or from local resources through NRO accounts.

2. Foreign Currency Loans in India
- Against security of funds in FCNR-B deposits.
- Maturity of loan should not exceed due date of deposits.
- Repayment from Fresh remittances or from maturity proceeds of

deposits.

3. Loans to 3rd Parties provided
- There is no direct or indirect consideration for NRE depositor agreeing to pledge his FD.
- Margin, rate of Interest and Purpose of loan shall be as per RBI guidelines.

- The loan will be utilized for personal purpose or business purpose and not for re-lending or carrying out Agriculture/Plantation/Real estate activities.
- Loan documents will be executed personally by the depositor and Power of attorney is not allowed.

4. Housing Loans to NRIs : HL can be sanctioned to NRIs subject to following conditions:
- Quantum of loan, Margin and period of Repayment shall be same as applicable to Indian resident.
- The loan shall not be credited to NRE/FCNR account of the customer.
- EM of IP is must and lien on assets.
- Repayment from remittance abroad or by debit to NRE/FCNR account or from rental income derived from property.

Portfolio Investment Scheme for NRIs

RBI has permitted NRIs to invest in PIS subject to following conditions:
Investment on repatriation as well as non-repatriation basis.
Purchase/Sale of shares and debentures
Through Regd. Brokers
Amount is routed through designated branch.
Only delivery based transactions
Investment on Repatriation basis can be made out of inward remittances or out of NRE/FCNR deposits.
Investment on Non-Repatriation basis can be made out of NRO deposits besides NRE/FCNR deposits.
Ceiling PER Investor
5% of paid up capital of Indian Company or 5% of Value of each issue of convertible debentures.
Ceiling PER Investor Company
10% of paid up capital of Indian Company or 10% of Value of each issue of convertible debentures.

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RBI controls Foreign Exchange

RBI is empowered to
Control and regulate Foreign Exchange Reserves
Supervise Foreign Exchange dealings
Maintain external value of Rupee
FERA was replaced by FEMA in the year 1999.

FEMA provisions

The important FEMA guidelines with regard to Foreign exchange are as under:
1. No drawl of exchange for Nepal and Bhutan
2. If Rupee equivalent exceeds Rs. 50000/-, payment by way of crossed Cheque.
3. During visit abroad, one can carry foreign currency notes up to **USD 3000** or equivalent. For Libya and Iraq, the limit is **USD5000** and the entire amount for **Iran and Russian** states.
4. Indian citizens can retain and possess foreign currency up to **USD**

2000 or its equivalent.
5. Unspent currency must be surrendered within a period of **180 days** after arrival in India.

Basic Travel Quota (BTQ)

Purpose of Visit Up to USD or equivalent
Personal/Tourism 10000 per financial year
Business Purpose 25000 per visit
Seminars/conferences 25000 per visit
Employment/Immigration 100000
Studies 100000 per academic year
Medical 100000
Donations/Gifts 5000 per donor per year
Consultancy services 100000 per project
Debit Credit/Credit Card As per BTQ as above

***AD can release Foreign Exchange 60 days ahead of journey**

LRS (Liberalized Remittance Scheme)

The scheme is meant for Resident Indians individuals. They can freely remit up **USD 125000** per financial year in respect of any current or capital account transaction without prior approval of RBI. The precondition is that the remitter should have been a customer of the bank for the last 1 year. PAN is mandatory.

Not Applicable

The scheme is not applicable for remittance to Nepal, Bhutan, Pak, Mauritius or other counties identified by FATF.

The scheme is not meant for remittance by Corporate.

Latest Guidelines

The scheme should not be used for making remittances for any prohibited or illegal activities such as margin trading, lottery etc., as hitherto.

Resident individuals have now been allowed to set up Joint Ventures (JV) / Wholly Owned Subsidiaries (WOS) outside India for

bonafide business activities outside India within the limit of USD 125000

The limit for gift in Rupees by Resident Individuals to NRI close relatives and loans in Rupees by resident individuals to NRI close relatives shall accordingly stand modified to USD 1,25,000 per financial year.

RBI has clarified that Scheme can now be used for acquisition of IP outside India.

Import and Export of Indian Rupees

Any person resident in India
a) May take outside India (other than Nepal and Bhutan) currency notes up to Rs. 25000/- or
b) May bring into India (from country other than Nepal and Bhutan) currency notes up to Rs. 25000/-
Any person Resident Outside India (Not being citizen of Pak and Bangladesh)
a) May take outside India currency up to Rs. 25000/-
b) May bring into India currency notes up to 25000/-
(Previously, the limit was Rs. 10000/-)
Any amount can be taken out while going to Nepal and Bhutan in any denomination. (Prev. Notes up to 100 denomination were allowed)

Restrictions Customer is required to furnish PAN No. for cash remittance beyond 25000/-.

If rupee equivalent is 50000/- and above, the entire payment has to be made by way of crossed cheque or DD.

RETURNS TO BE SUBMITTED TO RBI

Following important returns are submitted to RBI
R- Returns Forex Operations (Fortnightly)
BAL statement Balance in Nostro/Vostro account
STAT 5 Transactions in FCNR B accounts (Fortnightly)
STAT 8 Transactions in NRE/NRO accounts

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(Fortnightly
LRS Statement UP to USD 200000 (monthly)
Trade Credit Statement Buyers" and Suppliers" Credit
XOS O/S Overdue Export bills (6M overdue)
BEF Import Remittance effected but Bill of Entry
not submitted for >3M.
ETX Form Seeking relaxation from RBI after expiry of
12M when export proceeds are not received.

„
RFC accounts Resident Foreign Currency account is opened by Indian residents who were earlier NRIs and Forex is received by them from their overseas dues:

The accounts can be opened as SB/CA/FD type.
Proceeds are received from overseas.
Out of Monetary benefits accruing abroad
The funds are freely repatriable.
Minimum amount is USD 5000.

RFC- D accounts Resident Foreign Currency (Domestic) accounts are opened:

By Indian residents who visit abroad: and
Bring with them Foreign Exchange;
As honorarium, gift etc.
Unspent smoney can also be deposited.
These are CA nature accounts and no interest is paid.

Exchange Earners Foreign Currency

Exchange Earners Foreign Currency accounts can be opened by exporters. 100% export proceeds can be credited in the account which does not earn interest but this amount is repatriable outside India for imports **(Current Account transactions).**

1. Who can open: The account can be opened by any resident. This account will be opened by exporters.
2. Type of account: Non interest bearing current account (up to 31.10.08 FD account was also allowed)
3. Credits: 100%of foreign exchange earnings can be credited to this account.
4. Repatriation is allowed for permissible current account transaction and permissible capital account transaction.
5. Packing credit can be adjusted out of such funds.

Account holder : Exporters of goods and services, resident in India
Source of funds: Up to 100% of forex earnings can be kept in the account. But amount to be converted in rupees, latest by last day of next month.
Use of funds: Balance can be transferred to NRE/FCNR account on change of status from resident to non-resident. Funds can be used for adjustment of pre-shipment loans.
Loan: No loan can be allowed against the balances in such account.
Type of account: Current account, single or joint (FORMER or SURVIVOR) with close resident relatives.
Interest : No Interest is payable **LIBERALISED**

FEDAI – Foreign Exchange Dealers Association of India

Foreign Exchange association of India is a non-profit body established in 1958 by RBI. All public sector banks, Private Banks, Foreign Banks and Cooperative banks are its members. The functions of FEDAI are:

Forming uniform rules
Providing training to bankers; and
Providing guidance and information from time to time.

The important rules are:
1. Export TransactionsForex liability must be crystallized into Indian rupees on 30th day after expiry of NTP at TT selling rate(Notional Transit Period) in case of Sight bills and **on 30th day** after notional due date in case of Usance bills. **The rule has since been relaxed and bank can frame its own rule for nos. of days for crystallization.**
2. Concessional rate of interest is applied up to Notional due date or up to value date of realization of export dues (whichever is earlier)
3. Import Transactions: For retirement of Import bills whether under LC or otherwise, **Bill selling rate or Contracted selling rate** whichever is higher, will be applied.
DP Bills (sight) are retired after crystallization on 10th day after receipt.

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DA Bills are retired (crystallized) on Due Date.
4. All Foreign Currency bills under LC, if not retired on receipt, shall be crystallized into Rupee liability on **10th day** after date of receipt of documents at**Bill Selling Rate or** contracted rate whichever is higher.
Normal Transit Period is:
- 25 days for export bills,
- 3 days for Rupee bills drawn under LC and payable locally
- 7 days for rupee bills drawn under LC and payable at other centers
- 20 days for Rupee bills not drawn under LC.
- For exports to Iraq, normal transit period is 60 days.

Compensation on Delayed payment:
All Foreign Inward remittances up to **Rs.1.00 lac** should be converted into Indian Rupees immediately
The proceeds of any Inward remittance should be credited to the account within 10 days and advice of receipt is to be sent within 3 days, failing which, compensation @2% above SB rate will be paid to the beneficiary.
Forward Contracts
Exchange contracts will be for definite amount and period.
Contracts must state first and last date of contracts e.g. from 1-31 Jan or from 17th Jan to 16th Feb.
For contracts up to 1 month, option period for delivery may be specified.

In case of extension of contract, previous contract will be cancelled at TT Buying rate or TT selling rate as the case may be.
Overdue contracts are liable to be cancelled on **7th working day** after maturity date if no instructions are received. The contracts must state first and last date of the contract.
Banks are now free to fix their own rates of commission and margin etc.
AP may be imposed penalty up to 3 times of contravention amount. If amount is not quantifiable, up to 2.00 lac and up to 5000/- per day is imposed, if the contravention continues.

ECBs – External Commercial Borrowings

External Commercial Borrowings are medium and long term loans as permitted by RBI for the purpose of :
Fresh investments
Expansion of existing facilities
Trade Credit (Buyers" Credit and Sellers" Credit) for 3 years or more.
Automatic Rout
ECB for investment in Real Estate sector , Industrial sector and Infrastructure do not require RBI approval
It can be availed by Companies registered under Indian Company Act.
Funds to be raised from Internationally recognized sources such as banks, Capital markets etc.
Maximum amount per transaction is U**SD 20 million** with minimum average maturity of 3 years
Maximum amount per transaction is U**SD 750 million** with minimum average maturity of 5 years
.
All in cost ceiling is :
ECB up to 5 years : 6M LIBOR+350 bps.
ECBs above 5 years: 6M LIBOR+500 bps.
Approval Route
Under this route, funds are borrowed after seeking approval from RBI.
The ECBs not falling under Automatic route are covered under Approval Route.
Under this route, Issuance of guarantees and Standby LC are not allowed.
Funds are to be raised from recognized lenders with similar caps of all-in-cost ceiling.

ADRs –American Depository Receipts

American Depository Receipts are Receipts or Certificates issued by US

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Bank representing specified number of shares of non-US Companies.
Defined as under:

- These are issued in capital market of USA alone.
- These represent securities of companies of other countries.
- These securities are traded in US market.
- The US Bank is depository in this case.
- ADR is the evidence of ownership of the underlying shares.

Unsponsored ADRs
It is the arrangement initiated by US brokers. US Depository banks create such ADRs. The depository has to Register ADRs with SEC (Security Exchange Commission).
Sponsored ADRs
Issuing Company initiates the process. It promotes the company"s ADRs in the USA. It chooses single Depository bank. Registration with SEC is not compulsory. However, unregistered ADRs are not listed in US exchanges.

GDRs – Global Depository Receipts
Global Depository Receipt is a Dollar denominated instrument with following features:
1. Traded in Stock exchanges of Europe.
2. Represents shares of other countries.
3. Depository bank in Europe acquires these shares and issues "Receipts" to investors.
4. GDRs do-not carry voting rights.
5. Dividend is paid in local currency and there is no exchange risk for the issuing company.
6. Issuing Co. collects proceeds in foreign currency which can be used locally for meeting Foreign exchange requirements of Import.
7. GDRS are normally listed on "Luxembourg Exchange " and traded in OTC market London and private placement in USA.
8. It can be converted in underlying shares.

IDRs – Indian Deposits Receipts
Indian Depository Receipts are traded in local exchanges and represent security of Overseas Companies.
CDF (Currency Declaration Form)

CDF is required to be submitted by the person on his arrival to India at the Airport to the custom Authorities in the following cases:
1. If aggregate of Foreign Exchange including foreign currency/TCs exceeds USD 10000 or its equivalent.
2. If aggregate value of currency notes (cash portion) exceeds USD 5000 or its equivalent.

Form A1 and
Form A2
Form A1 is meant for remittance abroad to settle imports obligations. It is not required if value of imports is up to USD 5000.
Form A2 is meant for remittance abroad on account of any purpose other than Imports. It is not required if remittance is up to USD 25000.
LIBOR Rate London Interbank Offering rate is the rate fixed at 11 am (London time) at which top 16 banks in London offer to lend funds in interbank markets.

Interest Subvention on Export
Credit
RBI vide notification no. DBOD.Dir.BC.No.43/04.02.001/2013-14 dated 26.08.2013 has informed that Government has decided to increase the rate of interest subvention on the existing sectors from the present 2% to 3% with effect from August 1, 2013 on the same terms and conditions.
3. Accordingly, the interest rate chargeable to the exporters will be reduced as per Base Rate system in the existing sectors eligible for export credit subvention by the amount of subvention available, subject to a floor rate

of 7%. It should be ensured that the benefit of 3% interest subvention is passed on completely to the eligible exporters.

Foreign Currency Borrowingsby ADs from
Overseas
It has been decided to liberalize this facility further. Accordingly, AD Category

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- I banks may henceforth borrow funds from their Head Office, overseas branches and correspondents and overdrafts in Nostro accounts **up to a limit of 100 per cent of their unimpaired Tier I capital** as at the close of the previous quarter or **USD 10 million (or its equivalent**), whichever is higher, as against the existing limit of 50 per cent (excluding borrowings for financing of export credit in foreign currency and capital instruments).

Trade Credit – Revised RBI guidelines

Banks may approve availing of trade credit not exceeding USD 20 million up to a maximum period of five years (from the date of shipment) for companies in the infrastructure sector, subject to certain terms and conditions stipulated therein.

On a review, it has been decided to allow companies in all sectors to avail of trade credit not exceeding USD 20 million up to a maximum period of five years **for import of capital goods** as classified by Director General of Foreign Trade (DGFT).

Crystallization of Inoperative Foreign Currency Deposits

RBI has advised that AD will crystallize i.e. convert foreign currency deposit (with fixed maturity date) into INR, if remains **in-operative for 3 years** from date of maturity.

If a deposit account has not been operated for 10 years, the amount will be transferred to DEAF.

FOREIGN EXCHANGE

1. Global Foreign Exchange Markets

24 hour non-stop market:

The main feature of this market is that, it is continuous - i.e., open 24 hours a day. The time zones are as follows: The market begins with New York (6 p.m India time) , then Sydney, followed by Tokyo. When we come to work in the morning here in India, Tokyo is at lunch. The Frankfurt market opens at 10 a.m our time; then London (12.30 our time) and we go back full circle to New York again. This means that there is a price available always, anytime and you can transact whenever you want.

2. Introduction to Foreign Exchange

Foreign exchange rate is the value of a foreign currency relative to domestic currency. The exchange of currencies is done in the foreign exchange market, which is one of the biggest financial markets. The participants of the market are banks, corporations, exporters, importers etc. A foreign exchange contract typically states the currency pair, the amount of the contract, the agreed rate of exchange etc.

A foreign exchange deal is always done in currency pairs, for example, US Dollar – Indian Rupee contract (USD – INR); British Pound – INR (GBP - INR), Japanese Yen – U.S. Dollar (JPYUSD), U.S. Dollar – Swiss Franc (USD-CHF) etc. Some of the liquid currencies in the world are USD, JPY, EURO, GBP, and CHF and some of the liquid currency contracts are on USD-JPY, USD-EURO, EURO-JPY, USD-GBP, and USD-CHF.

In a currency pair, the first currency is referred to as the base currency and the second currency is referred to as the 'counter/terms/quote' currency. The exchange rate tells the worth of the base currency in terms of the terms currency, i.e. for a buyer, how much of the terms currency must be paid to obtain one unit of the base currency. For example, a USD-INR rate of Rs. 48.0530 implies that Rs. 48.0530 must be paid to obtain one US Dollar. Foreign exchange prices are highly volatile and fluctuate on a real time basis. In foreign exchange contracts, the price fluctuation is expressed as appreciation/depreciation or the strengthening/weakening of a currency relative to the other. A change of USD-INR rate from Rs. 48 to Rs. 48.50 implies that USD has strengthened/ appreciated and the INR has weakened/depreciated, since a buyer of USD will now have to pay more INR to buy 1 USD than before.

Let us first spend a little time in understanding what are the broad factors that affect Foreign Exchange and Money Markets?

EXCHANGE RATES IN THE LONG RUN: What determines Ex-rates?

Basically, the Supply and Demand for currency determines ex-rates, market forces, like any commodity or asset. We first look at ex-rates in the long-run (LR) and then ex-rates in the short-run (SR).

LAW OF ONE PRICE (LOP): starting point for understanding ex-rates in the LR. Also called the "price equalization principle": for homogeneous, identical goods, the price of the commodity should be the same (equalize) throughout the world, especially when barriers to trade, transactions costs and transportation costs are low. Says that foreign prices (Pf), domestic prices (Pd) and ex-rates (e) are linked through the Law of One Price which says: Pd ($) = e * Pf (£) , where e = $ / £. LOP says that similar products should sell for the same price in both countries, after converting the foreign price into dollars.

Example: Price of gold in U.S. = $260 (Pd) , Price of gold in Canada = C$400 (Pf) and e = $0.65 / C$.

LOP holds: $260 = ($.65/C$) x C$400, says that gold sells for the same price ($260/ounce) in both the U.S. and Canada, after converting the foreign price into $. The price of gold should equalize around the world and sell for about the same price everywhere: $ 260/ounce. What if somewhere in the world, P < $260/oz, what would happen? What if somewhere in the world, P > $260, what would happen? ARBITRAGE: Riskless profits from exploiting price discrepancies.

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Law of One Price would be restored, through an adjustment in gold prices here and in Canada, and through an adjustment in the ex-rate.
Law of One Price holds most strongly for: homogeneous, traded goods like commodities such as: gold, silver, wheat, steel, copper, oil, aluminum, cotton, etc. and financial assets like Treasury securities, bank CDs, etc. In fact, most of the currency trading is for financial transactions, not commodities.
Also Law of One Price assumes frictionless trading. If we introduce frictions like tariffs, taxes, transportation costs, commissions, shipping, insurance, etc., the Law of One Price may not always hold. Also, many goods and services may be non-tradeable items like haircuts and golf lessons. Law of One Price is a starting point for ex-rates, illustrates one aspect of how international trade affects ex-rates.

CAPITAL MOBILITY - There are now few restrictions on international capital mobility, and financial markets are international - international credit markets, bond markets, stock markets, etc. Bank deposits and treasury securities are considered perfect substitutes by international investors and they can now just shop the world credit and capital markets for the highest rate of return. For example, capital mobility allows a life insurance company/pension funds with millions of dollars to shop the world financial markets for the highest rate of return, they are not restricted to domestic markets anymore. Likewise, foreign investors can easily invest in the U.S. market, buy U.S. stocks, Treasury securities, corporate bonds, make deposits in U.S. banks, buy CDs here, money market instruments, etc. Capital mobility assumes that investment capital is internationally mobile, and capital flows to those countries and markets that offer the highest expected rates of returns.

Capital mobility, along with the Theory of Asset Demand, gives us insight into ex-rate determination in SR. The demand for domestic (dollar) assets and the demand for foreign (Euro, pound) assets is largely determined by the expected returns on those assets. When the expected return for U.S. assets (ius) is high relative to the expected return for foreign assets (if), the demand for U.S. assets will be high, and so will the demand for dollars. Therefore, it is the demand for domestic and foreign assets that creates demand for foreign currency (or the dollar), which then determines the value of foreign exchange in SR.
Reason: to take advantage of high interest rates in U.S. (U.K.), you first have to buy dollars (pounds). Also, we assume realistically that many financial assets are perfect (or very close) substitutes: Treasury securities, bank CDs, etc.
For example, you have $10m to invest in Treasury securities, so you consider 10 year government debt (T-bonds) issued by New Zealand, UK, Japan, Canada, Germany, Switzerland, Norway, etc., because they are all risk- free T-bonds. Or you consider, short term one year bank CDs in those same countries.
What do you base your decision on when considering these alternative investments in different countries? ___________________ and ___________________ .

Rate of return on a 1 year foreign investment to a U.S. investor has two components:
1) if = One year interest rate (nominal interest rate) on the foreign asset.
2) (F - E) / E = Expected rate of appreciation (%) or depreciation (%) of the foreign currency over the next year, where F = forward ex-rate and E = spot ex-rate

Examples:
a) E = $1.50/£ and F360 = $1.605/£. Pound is expected to appreciate by 7% over the next year.
b) E = $1.50/£ and F360 = $1.395/£. Pound is expected to depreciate by 7% over the next year.

You are really making two investments: 1) you are investing in the foreign asset (i) and 2) you are "investing" in the foreign currency £ (%F). For example, assume the one year foreign interest rate in UK (if) = 10%, you get a 10% guaranteed nominal return for the next year. If the pound appreciates by 7% versus the dollar, you get an additional return of 7%, for a total dollar return of 17%. The UK government paid you 10% nominal return, and you benefited over the next year by holding a foreign currency that appreciated by 7% relative to the dollar.
Investment process: You take $ and buy £ to buy the UK T-bill. After one year you get your proceeds in £ in UK and sell the pounds for $. Since the pound is

7% stronger than it was a year

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ago, you gained an additional 7% by holding a pound-denominated asset because the pound got stronger by 7%.

If the British pound depreciates by 7% over the next year, you lose 7% on your total return and you end up with 10% (nominal rate) MINUS 7% (depreciation of the pound), for a total dollar return of 3% (10% - 7% = 3%). POINT: When investing in a foreign asset, you GAIN when the foreign currency APPRECIATES, and you LOSE when the foreign currency DEPRECIATES.

Formula for INTEREST RATE PARITY (IRP):

ius = if + (F - E) / E

if = Nominal return on foreign asset for period t

ius = Nominal return on domestic asset for period t

where the domestic asset and foreign asset are perfect or close substitutes (T-bills, bank CDs, etc.) E = spot ex-rate

F = forward ex-rate for period t

(F - E) / E = % Appreciation (or % Depreciation) of the Foreign Currency over the relevant period. ius = Effective dollar return to US investor for an investment in a foreign country

Interest Parity implies that: (ius - if) = (F - E) / E meaning that:

For similar assets in two different countries, the difference in nominal interest rates reflects the expected change in the ex-rate.

Example: Interest rates for 1 year Tbills in US are 8%, 1 year interest rates in Germany are 6%, and 1 year interest rates in Canada are 10%.

US vs. Germany: 8% (US) = 6% (Germany) + 2% (Appreciation of DM)

Parity condition implies equality of returns in both countries after taking into account the appreciation or depreciation of the foreign currency. You can get an 8% dollar return in the U.S. or an effective 8% dollar return in Germany (6% nominal + 2% appreciation).

or

(8% - 6%) = +2% Appreciation of the German mark.

The difference in 1 year nominal interest rates between US and Germany (+2%) reflects an expected appreciation of the DM of 2% over the next year. A U.S. investor will get an effective 8 percent return in either country, after taking into account the change in foreign currency. (For a German investor, they can get 6% in Germany, or an 8% nominal dollar return in U.S. MINUS a - 2% depreciation of the dollar for a 6% return in either country.)

US vs. Canada: 8% (U.S.) = 10% (Canada) - 2% (Depreciation of the C$).

or

(8 - 10%) = -2% Depreciation of the C$.

A U.S. investor will get a dollar return of 8% in the U.S., or a 10% return in Canada MINUS -2% depreciation of the Canadian dollar, for an effective dollar return of 8%. Or the difference in nominal interest rates (-2%) reflects an expected depreciation of the foreign currency, the C$.

If bank deposits are perfect substitutes and there is international capital mobility, and there are active forward markets for foreign currency, interest rate parity has to hold. Reason: you can cover yourself with a forward contract.

Other Long Run Factors:-

I. MACRO - ECONOMIC FUNDAMENTALS:

1.GDP Growth :

This is the primary indicator of economic growth. This gives a bird's eye view of the economy and its performance.It is the value of all goods and services produced by the nation's labour and capital inputs. It is broken further into private consumption expenditure, investment expenditure, government consumption expenditure and net trade balance.

2.Balance of Payments:

This has three components:-

i.Trade Gap (Imports less Exports)

ii.Current Account balance (trade gap including invisibles)

iii.Capital Flows

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This gives an indication for future exchange rate policy especially for less developed markets. Currency devaluation assists exports by making them more competitive and at the same discouraging imports by making them more expensive.

3. Industrial production / Capacity Utilisation/Unemployment: This indicates the health of the manufacturing sector of the economy.

4. Structural considerations:

i.Reserve Composition (Short /Long Term liabilities):

This indicates the extent of hot money that constitutes your reserves. A higher percentage of short term obligations tends to make the economy more vulnerable to exchange rate volatility and also a degree of uncertainty as regards the ability to renew these short term liabilities.

ii.Import elasticity (Dependence on Oil imports):

Volatility in oil prices brings a greater degree of uncertainty to economies dependent to a large extent on oil imports.

iii.Structure of Exports - whether import dependent :

This relates to the nature of products exported and their susceptibility to the relative exchange rate.

iv.Nature of Inflation (Demand pull/Cost push):

Inflation resulting due to excessive demand factors tends to have more impact on monetary policy than those caused by higher input costs.

v.Market Liquidity /yield curve dynamics:

This is more relevant in less developed markets. Markets with poor liquidity tend to be more volatile.

vi.Strength of the Financial System - (Banking sector Capitalisation , Non Performing Assets (NPAs)

These factors also tend to influence interest rate policies in many countries.

6. Government Policy :

This is again relevant in more controlled markets. The attitude of the government regarding their policy focus - Pro reform v/s greater controls. A case in example is Indonesia. The country had to resort back to capital controls to protect its exchange rate.

Expectation against reality - Speed of implementation and Government commitment:

This tends to affect sentiment more than anything else. India's divestment policy is a good case in example where political intent is lacking.

II. SHORT RUN FACTORS:

Demand - Supply mismatches: This could lead to some short term volatility in the exchange rate.

Comments by key people: The Japanese Yen is a typical case in example. Sakakibara , the then Vice Finance Minister could move markets by his comments on the currency (He was termed Mr. Yen by market players)

Central Bank Intervention: During times of excessive depreciation/appreciation, the Central bank may intervene to bring stability to the markets.

Political Uncertainties and other factors:

Assassinations / Scandals War / natural Disasters : Flight to Quality :

III. TECHNICAL MARKET FACTORS:

Technical Factors, in market parlance, are essentially based on the fact that history tends to repeat itself. By looking at past data, one can forecast exchange rates. There are various indicators, some of which have been listed below, the details of which are beyond the scope of this module. A significant percentage of market participants use these techniques for their trading and hedging purposes.

Break Of Key Support / Resistance Levels

Pattern Formations like S-H-S(Shoulder - Head - Shoulder), Triangles Extreme Overbought / Oversold

conditions

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Profit Taking

This concludes our first chapter. We have given you an idea of what affects Currency and Interest Rate Markets. However , as we said before, you may find some contradictions in reality , but these are what make these markets so much more interesting and uncertain to predict.It is advised that you go through the section thoroughly, and revise if necessary.

It is important to mention here that the data released must be analysed with respect to the following : As compared with the prior period…

As compared to the same period in the previous year (to look for seasonality if any)

As compared to market expectations. This is important as the market discounts certain extraordinary factors and rates move if actual data differ from expectations rather than based on absolute numbers. For e.g., spiraling oil prices during August 2000 affected inflation numbers adversely. With a trader's perspective, one must realise that markets tend to react in a flash, and the early bird gets to make the big bucks.

2. Foreign Exchange Rates & Arithmetic

Exchange Rate Regime : The exchange rate regime is a method through which a country manages its currency in respect to foreign currencies and the foreign exchange market.

Fixed Exchange Rate: A fixed exchange rate is a type of exchange rate regime in which a currency's value is matched to the value of another single currency or any another measure of value, such as gold. A fixed exchange rate is also known as pegged exchange rate. A currency that uses a fixed exchange rate is known as a fixed currency. The opposite of a fixed exchange rate is a floating exchange rate.

Floating Exchange Rate: A Floating Exchange Rate is a type of exchange rate regime wherein a currency's value is allowed to fluctuate according to the foreign exchange market. A currency that uses a floating exchange rate is known as a floating currency. A Floating Exchange Rate or a flexible exchange rate and is opposite to the fixed exchange rate.

Linked Exchange Rate: A linked exchange rate system is used to equalize the exchange rate of a currency to another. Linked Exchange Rate system is implemented in Hong Kong to stabilise the exchange rate between the Hong Kong dollar (HKD) and the United States dollar (USD).

QUTOATION STYLE:

Various kinds of quotes are described in the following sections.

American vs. European Quote

A quote can be classified as European or American only if one of the currencies is the dollar. An American quote is the number of dollars expressed per unit of any other currency, while a European quote is the number of units of any other currency expressed per dollar. For example, Rs. 48.28/ $ is a European quote, while $1.6698/£ is an American quote. In almost all the countries, most of the exchange rates are quoted in European terms. The British pound, the Irish pound and the South African rand are a few examples of currencies quoted in American terms.

Direct vs. Indirect Quote

Direct quote: In this case there is one unit of foreign currency and corresponding units of home currency. Examples of direct quotes in India:

1$ = Rs.46 1£ = Rs.68 1 Euro = Rs.54

Indirect quote: In this case there is one unit of home currency and corresponding units of foreign currency. Examples of indirect quotes in India:

Re. 1 = $ 0.0250 Re. 1 = £ 0.0122 Re. 1 = Euro 0.0185

OR Indirect quote = $\frac{1}{\text{Direct quote}}$

Here, the bank would be buying dollars @ $2.1998/Rs.100 and selling dollars @ $2.1978/Rs.100.
The corresponding direct quote would be:

$ 1=Rs. 45.4586/45.5000

Here, the bank would be buying dollars @ Rs. 45.4586/$ and selling dollars @ Rs. 45.5000/$.

Before August 2, 1993, the indirect methods of quoting exchange rates used to be followed in India.
Since that date, however, the direct quote is being used. In other countries, the concepts of

American and European quotes are more popular in comparison to direct and indirect quotes.

Example (A) Example Convert the following direct quotes (in India) into indirect quotes:
1$ = Rs.40 1£ = Rs.82
Answer: Indirect quotes (in India) Re. 1 = $ 1/40 i.e. $ 0.0250

Re. 1 = £ 1/82 i.e. £ 0.0122

Example (B) Convert the following indirect quotes (in India) into direct quotes:
Re. 1 = $ 0.0222 Re. 1 = £ 0.0122
Answer : Direct quotes (In India) 1$ = Rs.1 / 0.0222 i.e. Rs.45 1£ = Rs.1/ 0.0122 i.e.

Rs.82

Bid and Ask Rate

In the quotes given above, there was one single rate at which the currencies were being bought and sold. For example, the rupee-dollar exchange rate was given as $1=Rs. 45.50/.617. In reality, the rate at which a bank is ready to buy a currency will be different from the rate at which it stands ready to sell that currency. These rates are called the bid rate(bank will buy foreign currency) and the ask (bank will sell foreign currency) rates respectively. The difference in these rates represents the cost the bank incurs in these transactions, a small return on the capital employed, and the compensation for the risk it takes. This risk arises on account of the possibility of the exchange rate moving in an unfavorable direction before the bank is able to offset the transaction. The single rate mentioned above is generally the mid-rate, i.e. the arithmetic mean of the bid and the ask rates. The difference between the bid rate and the ask rate is called the bid-ask

Examples:
1 USD = 1.2800 CHF
USD is the fixed currency i.e currency being priced, in terms of CHF ; so, CHF is the variable currency. Now, if 1.7925 USD = 1 GBP
In this case USD becomes the variable currency and GBP the fixed currency.
('USD' = U.S dollar, 'CHF' = Swiss Franc, 'GBP' = Pound Sterling, 'AUD'= Australian dollar)

CROSS CURRENCY RATES

Before one currency gets converted into another, in most cases, it first gets converted into US Dollars. However, all those currency conversions that happen in foreign exchange, wherein one currency directly gets converted into the other currency (without converting it first to USD), are called currency cross rates, i.e, EUR (euro) / GBP (Great British pound) or GBP / Yen (Japanese yen) or GBP/Rs., Euro/Rs. etc. Sometimes we may not get a quote from market regarding our currency with foreign currency and hence we need to get by cross currency only.

How to calculate Cross currency rates?
Step 1: Review the five "major" crosses that are used to determine cross currencies. They are:
EUR/USD (euro/U.S. dollar)
GBP/USD (Great British Pound/U.S. dollar)
USD/CHF (U.S. dollar/Swiss franc)
USD/JPY (U.S dollar/Japanese Yen)
AUD/USD (Australian dollar/U.S. dollar)

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Step 2 : Determine the rates for the two currencies you want to calculate a cross currency rate for. Let's say you want to calculate a cross rate for the EUR/CHF and the current quote for EUR and CHF is:
EUR/USD = 1.2060
USD/CHF = 1.5080

Step 3: Calculate the currency cross. Multiply the first currency in the pair by the second currency in the pair. For instance, the EUR/CHF cross is calculated by multiplying the currency rate for EUR by the currency rate for CHF. The calculation is: 1.2060 x 1.5080 = 1.8186

Example a. 1USD = Rs. 40.00 1USD = CHF 1.40 1 CHF = Rs. ?

Answer:

1$	= Rs.40.00	(It is Rs./$)
1$	= CHF 1.40	(It is CHF/$)
Re. 1 = $ 0.0250		(It is $/Re)
1CHF = $ 0.71429		(It is $/CHF)

We have to find (Rs./CHF)

$$\frac{Rs}{CHF} = \frac{Rs.}{\$} \times \frac{\$}{CHF} = 40 \times 0.71429 = Rs.28.5714$$

Example b: Given the following rates, find 'bid' and 'ask' rates for CY in terms of rupees.
1 USD = 5.7040 – 5.7090 CY
1 USD = 40.30 - 40.50 Rupees

Answer:

1$	= CY 5.7040/5.7090	(it is CY/$)
1$	= Rs.40.30/40.50	(it is Rs./$)
1CY	= $(1/5.7090) / (1/5.7040)	(it is $/CY)
1 Re.	= $(1/40.50) / (1/40.30)	(it is $/ Rs.)

We have to find Rs./CY.

$$Rs./CY = \frac{Rs.}{\$} \times \frac{\$}{CY}$$

Rs. / CY (bid) = (40.30) X (1 /5.7090) = 7.0590
Rs. / CY (ask) = (40.50) X (1/5.7040) = 7.1003
Rs. / CY = 7.0590 / 7.1003

1 CY = Rs.7.0590 / Rs.7.1003

What are the basic types of Foreign Exchange transactions?

Types of Transactions

Foreign exchange transactions can be classified on the basis of the time between entering into a transaction and its settlement. They can basically be classified into spot and forward contracts. Spot transactions are those, which are settled after 2 business days from the date of the contract. A forward contract (also called an outright forward) is one where the parties to the transaction agree to buy or sell a commodity (here, a currency) at a predetermined future date at a particular price. This future date may be any date beyond two business days. The price and the terms of delivery and payment are fixed at the time of entering into the contract. In the forex markets, forward contracts generally mature after 1, 2, 3, 6, 9, or 12 months.

A forward contract is normally entered into to hedge oneself against exchange risk (i.e., the uncertainty regarding the future movements of the exchange rate) . By entering into a forward contract, the customer locks-in the exchange rate at which he will buy or sell the currency.

Forward rates can be derived from interest rates of the two currencies. It is basically a function of the interest rate differential between the currencies. Let us take an example :

MARKET RATES :

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3 Month GBP : 4.0 %

3 Month USD : 1.0 %

Spot GBP / USD : 1.7900

Interest Rate Differential -------------------------> Exchange Rate Differential

(Spot Rate X Int. Rate Differential)/100 X No. of Months Forward/12 Months

To make it more scientific you can take the actual number of days in the month.

12 months is taken as 365 for GBP and INR and 360 for other currencies as per market practice.

$$\frac{1.7900 * 3}{100} \times \frac{3}{12} = 0.0134$$

SPOT RATE USD 1.7900

A currency is said to be at premium against another currency if it is more expensive in the forward market than in the spot market. In this case, its forward rate will be higher than its spot rate. This happens when the future spot rate is expected to be higher than the current spot rate. Conversely, a currency is said to be at a discount if it is cheaper in the forward market than in the spot market. In this case, its forward rate will be lower than its spot rate. This happens when the future spot rate is expected to be lower than the current spot rate. Let us assume the Rs/$ quotes to be:

Rs/$: 45.42/44

3-m Rs/$: 46.62/70

Here, the bank is ready to give only Rs. 45.42 currently in exchange for a dollar, while it is ready to give Rs. 46.62 after 3 months. Similarly, the bank is charging only Rs. 45.44 for selling a dollar now, while it is charging Rs. 46.70 for a delivery 3 months hence. So the dollar is expected to be more expensive in the future, and hence is at a premium against the rupee. On the other hand, the rupee is expected to be cheaper in the future and hence is at a discount against the dollar.

Let us now assume the $/£ quotes to be:

$/£ : 1.6721/26

3-m $/£ : 1.6481/92

Here the dollar is at a premium against the pound, while the pound is at a discount against the dollar. It is possible that a currency may be at a premium against one currency, while being at a discount against another at the same time. It is also possible that a currency be at a premium against another for a particular forward maturity, while being at a discount against the same currency for another forward maturity. E.g., the $/£ quotes may be:

$/£ : 1.6721/26

2-m $/£ : 1.6726/34

3-m $/£ : 1.6481/92

Here, the pound is at a premium against the dollar for the 2-month maturity, but at a discount for the 3-month maturity. It is also possible to have such a situation where a currency is at a premium against another for a particular forward maturity, but a discount between two forward maturities. E.g., the $/£ quotes may be:

$/£ : 1.6721/26

1-m $/£ : 1.6730/37

2-m $/£ : 1.6726/35

Here, the pound is at a premium against the dollar for both the forward maturities, but at a discount between the one -month and the two-month maturities.

Forward premium/discount is generally calculated as percentage per annum.

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= (Forward rate-Spot rate) 12/n. *100
Spot rate

Where 'n' indicates the number of months till maturity of the forward contract Margin by bank :-

Exchange margin is the extra amount or percentage charged by the bank over and above the rate quoted by bank.
When we are given the Spot rate / forward rate with margin for buying rate and margin for selling rate then effective rate will be calculated as:

Deduct margin from buying rate to get desired exchange rate. Hence, Now, buying rate will be = Bid rate – exchange margin

Example :- Given $ = Rs. 54.480/.900 and Margin is 0.08% then the Bid rate after margin will be:
$ = Rs.54.480 – 0.0435 (54.480 *0.08%) OR Rs. 54.480 (1-0.0008)
= Rs. 54.436

Add margin to selling rate to get the desired rate. Hence, Now, selling rate = Ask rate + exchange margin

Example: Given $ = Rs. 54.480/.900 and Margin is 0.08% then the Ask rate after margin will be:
$ = Rs.54.900 + 0.0439 (54.900 *0.08%) OR Rs. 54.900 (1 + 0.0008)
= Rs. 54.9439

Practice Problems:-

Q.1 An Indian firm is interested in purchasing 5m Chinese Yuan. The following quotations have been given by two different banks.

Bank A : 1 Pound = Rs. 79.89 / 80.00
1 Pound = CY 12.50 / 12.60
Bank B : 1 CY = $0.1598 – 0.1600
1 $ = Rs.40.00 / 40.05

Advise the Indian firm.

Answer :-

Two Alternatives (i) 5 Million CY can be purchased for 50,00,000 / 12.50 i.e. £ 4,00,000. This amount of £ can be purchased for 4,00,000x80 i.e. Rs.3,20,00,000
(ii) 5 Million CY can be purchased for 50,00,000 x0.1600 i.e. $ 8,00,000. This amount of $ can be purchased for 8,00,000 x 40.05 i.e. Rs. 3,20,40,000.
First alternative is recommended.

Q.2 An exporter customer requests a bank to sell 25,00,000 Singapore Dollar (SGD) . The inter-bank market rates are as follows:

Mumbai	US$ 1=	Rs.45.85/45.90
London	Pound 1=	USD 1.7840/1.7850
	Pound 1=	SGD 3.1575/3.1590

The bank wishes to retain an exchange margin of 0.125%. (Calculate rate in multiples of .0001).
How many Rupees the exporter will receive?

Answer:-

1$ = Rs.45.85/45.90……....................... (It is Rs./$)
1Re = $(1/45.90) / (1/45.85) (It is $/Re)
1 £ = $1.7840/1.7850…… ………………… (It is $/£)
1 $ = £ (1/1.7850) / (1/1.7840)………… (It is £/$)
1 £ = SGD 3.1575/ 3.1590………...........(It is SGD/£)
1SGD = £ (1/3.1590) / (1/3.1575)………… .(It is £/SGD)

Computation of SGD rate i.e. Rs/SGD.(The bank will be purchasing SGD, hence we have to calculate 'bid' rate.)

RS = RS. X $ X £

SGD $ £ SGD

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Rs. (bid) = 45.85 X 1.7840 X (1/3.1590) = Rs.25.8931307375

SDG

Taking bank margin into consideration bid rate per SGD: Rs.25.8931307375(1 -0.00125) i.e.

Rs.25.860764324. Total receipt = 6,46,51,911

Q.3. If the spot price for USD/EUR = 0.7395, then this means that 1 USD = .7395 EUR. The interest rate in Europe is currently 3.75%, and the current interest rate in the United States is 5.25%. Calculate the 1year forward rate.

Forward Exchange Rate = $\frac{S(1+rq)n}{(1+rb)n}$

S = Spot Price rq = Interest Rate of Quote Currency rb = Interest Rate of Base Currency

n = Number of Compounding Periods

$$= \frac{0.7395(1+0.0375)1}{(1+0.0525)1}$$

$$= \frac{0.7395 * 1.0375}{1.0525} = 0.7290$$

Thus, the forward exchange rate is 1 USD = 0.7290 (rounded) Euro, or simply, the forward rate.

Q.4. Calculate how many British pounds a London based firm will receive or pay for its following four foreign currency transactions:

(i) The firm receives dividend amounting to Euro 1,20,000 from its French Associate Company.

(ii) The firm pays interest amounting to 2,00,000 Yens for its borrowings from a Japanese Bank.

(iii) The firm exported goods to USA and has just received USD 3,00,000.

Given:

1$ = £0.50/0.51 1 Euro = £0.60/0.61 1 SGD = £0.39 /0.40

1 Yen = £0.0049 / 0.0050

(i) Foreign Exchange Rate: 1 Euro = £0.60/0.61

The firm shall be selling Euros; the bank shall be buying the Euro @ £0.60. The firm will receive 1,20,000 x 0.60 i.e. £72,000.

(ii) Foreign Exchange Rate : 100 Yens = £0.0049 / 0.0050

The firm shall be buying the Yens; the bank shall be selling the Yens @ £0.0050. The firm will pay 2,00,000 x 0.0050 i.e. £ 1,000.

(iii) Foreign Exchange Rate : 1 $ = £0.50/0.51

The firm shall be selling $; the bank shall be buying the $ @ £0.50. The firm will receive 3,00,000 x 0.50 i.e. £ 1,50,000.

(iv) Foreign Exchange Rate : 1 SGD = £0.39 /0.40

The firm shall be buying the SGD; the bank shall be selling the SGD @ 0.40. The firm will pay 4,00,000 x 0.4000 i.e. £ 1,60,000

Q 5. A person has to pay $ 13750 after three months today. Spot Rate: Re l = $ 0.0275. Rupee is likely to depreciate by 5% over three months. What is likely forward rate?

Answer: Rupee is left had currency. It is at discount. Amount of discount should be deducted from right hand currency for estimating the forward rate.

Hence forward rate is: Re. 1 = $ 0.0275 - $ 0.0275 (5/100) i.e. 0.026125.

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CHAPTER 2

FOREX DERIVATIVES

The financial environment today has more risks than earlier. Successful business firms are those that are able to manage these risks effectively. Due to changes in the macroeconomic structures and increasing internationalization of businesses, there has been a dramatic increase in the volatility of economic variables such as interest rates, exchange rates, commodity prices etc. Firms that monitor their risks carefully and manage their risks with judicious policies enjoy a more stable business than those who are unable to identify and manage their risks.

There are many risks which are influenced by factors external to the business and therefore suitable mechanisms to manage and reduce such risks need to be adopted. One of the modern day solutions to manage financial risks is ‘hedging’. Before trying to understand hedging as a risk management tool, we need to have a proper understanding of the term ‘risk’ and the various types of risks faced by firms.

What is risk?

Risk, in simple terms, may be defined as the uncertainty of returns. Risks arise because of a number of factors, but can be broadly classified into two categories: as business risks and financial risks.

Business risks include strategic risk, macroeconomic risk, competition risk and technological innovation risk. Managers should be capable of identifying such risks, adapting themselves to the new environment and maintaining their competitive advantage.

Financial risk, on the other hand, is caused due to financial market activities and includes liquidity risk and credit risk.

Risk Management

An effective manager should be aware of the various financial instruments available in the market for managing financial risks. There are many tools for the same and a judicious mix of various tools helps in efficient risk management.

Since the early 1970s, the world has witnessed dramatic increases in the volatility of interest rates, exchange rates and commodity prices. This is fuelled by increasing internationalization of trade and integration of the world economy, largely due to technological innovations. The risks arising out of this internationalization are significant. They have the capacity to make or break not only businesses but also the economies of nations. However, financial institutions are now equipped with tools and techniques that can be used to measure and manage such financial risks. The most powerful instruments among them are derivatives. Derivatives are financial instruments that are used as risk management tools. They help in transferring risk from the risk averse to the risk taker.

Derivatives are financial contracts whose value is determined from one or more underlying variables, which can be a stock, a bond, an index, an interest rate, an exchange rate etc. The most commonly used derivative contracts are forwards and futures contracts and options. There are other types of derivative contracts such as swaps, options, etc.

Currency derivatives can be described as contracts between the sellers and buyers whose values are derived from the underlying which in this case is the Exchange Rate. Currency derivatives are mostly designed for hedging purposes, although they are also used as instruments for speculation. Currency markets provide various choices to market participants through the spot market or derivatives market. Before explaining the meaning and various types of derivatives contracts, let us present three different choices of a market participant.

The market participant may enter into a spot transaction and exchange the currency at current time. The market participant wants to exchange the currency at a future date. Here the market participant may either:

• Enter into a futures/forward contract, whereby he agrees to exchange the currency in the future at a price decided now, or,

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1. Buy a currency option contract, wherein he commits for a future exchange of currency, with an agreement that the contract will be valid only if the price is favorable to the participant.

Forward Contracts : Forward contracts are agreements to exchange currencies at an agreed rate on a specified future date. The actual settlement date is more than two working days after the deal date. The agreed rate is called forward rate and the difference between the spot rate and the forward rate is called as forward margin. Forward contracts are bilateral contracts (privately negotiated), traded outside a regulated stock exchange and suffer from counter-party risks and liquidity risks. Counter Party risk means that one party in the contract may default on fulfilling its obligations thereby causing loss to the other party.
In the previous chapter we have seen how to calculate the forward rates.

Example: Forward Discount/ Premium
If the ninety day ¥ / $ forward exchange rate is 109.50 and the spot rate is ¥ / $ = 109.38, then the dollar is considered to be "strong" relative to the yen, as the dollar's forward value exceeds the spot value. The dollar has a premium of 0.12 yen per dollar. The yen would trade at a discount because its forward value in terms of dollars is less than its spot rate.

The annualized rate can be calculated by using the following formula:
Formula :-

$$\text{Annualized Forward Premium} = \frac{\text{Forward Price} - \text{Spot Price}}{\text{Spot Price}} \times \frac{12}{\text{\# of months forward}} \times 100\%$$

Answer:

((109.50 – 109.38 ÷ 109.38) × (12 ÷ 3) × 100% = 0.44%

Similarly, to calculate the discount for the Japanese yen, we first want to calculate the forward and spot rates for the Japanese yen in terms of dollars per yen.
Those numbers would be (1/109.50 = 0.0091324) and (1/109.38 = 0.0091424), respectively.
So the annualized forward discount for the Japanese yen, in terms of U.S. dollars, would be:
((0.0091324 – 0.0091424) ÷ 0.0091424) × (12 ÷ 3) × 100% = -0.44%

See Chapter FEDAI rules for more calculations & situations of forward contract.

International Swaps and Derivatives Association - ISDA
An association created by the private negotiated derivatives market that represents participating parties. This association helps to improve the private negotiated derivatives market by identifying and reducing risks in the market.

Futures Contracts (Please also refer more on this in chapter Treasury Products in Module C of this notes)
Futures contracts are also agreements to buy or sell an asset for a certain price at a future time. Unlike forward contracts, which are traded in the over- the-counter market with no standard contract size or standard delivery arrangements, futures contracts are exchange traded and are more standardized. They are standardized in terms of contract sizes, trading parameters, settlement procedures and are traded on a regulated exchange. The contract size is fixed and is referred to as lot size.
Since futures contracts are traded through exchanges, the settlement of the contract is guaranteed by the exchange or a clearing corporation and hence there is no counter party risk.
Exchanges guarantee the execution by holding an amount as security from both the parties. This amount is called as Margin money. Futures contracts provide the flexibility of closing out the

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contract prior to the maturity by squaring off the transaction in the market. Table will draws a comparison between a forward contract and a futures contract.

Short Currency future hedge   Long Currency future hedge

I) Currency Futures in India:-

A futures contract is a standardized contract, traded on an exchange, to buy or sell a certain underlying asset or an instrument at a certain date in the future, at a specified price. When the underlying asset is a commodity, e.g. Oil or Wheat, the contract is termed a "commodity futures contract". When the underlying is an exchange rate, the contract is termed a "currency futures contract". Both parties of the futures contract must fulfill their obligations on the settlement date.

Currency futures are a linear product, and calculating profits or losses on these instruments is similar to calculating profits or losses on Index futures. In determining profits and losses in futures trading, it is essential to know both the contract size (the number of currency units being traded) and also the "tick" value.

A tick is the minimum size of price change. The market price will change only in multiples of the tick. Tick values differ for different currency pairs and different underlyings. For e.g. in the case of the USDINR currency futures contract the tick size shall be 0.25 paise or 0.0025 Rupee. To demonstrate how a move of one tick affects the price, imagine a trader buys a contract (USD 1000 being the value of each contract) at Rs. 44.7500. One tick move on this contract will translate to Rs.44.7475 or Rs.44.7525 depending on the direction of market movement.

The contract amount (or "market lot") is the minimum amount that can be traded. Therefore, the profit/loss associated with change of one tick is: tick x contract amount The value of one tick on each USDINR contract is Rupees 2.50 (1000 X 0.0025). So if a trader buys 5 contracts and the price moves up by 4 ticks, he makes Rupees 50.00 (= 5 X 4 X 2.5)

(Note: The above examples do not include transaction fees and any other fees, which are essential for calculating final profit and loss).

Futures terminology:-

Some of the common terms used in the context of currency futures market are given below:

• Spot price: The price at which the underlying asset ($, £, €, ¥ etc.) trades in the spot market.

• Futures price: The current price of the specified futures contract.

• Contract cycle: The period over which a contract trades. The currency futures contracts on the SEBI recognized exchanges have one-month, two-month, and three-month up to twelve-month expiry cycles. Hence, these exchanges will have 12 contracts outstanding at any given point in time.

• Value Date/Final Settlement Date: The last business day of the month will be termed as the Value date / Final Settlement date of each contract. The last business day would be taken to be the same as that for Inter-bank Settlements in Mumbai. The rules for Inter-bank Settlements, including those for 'known holidays' and 'subsequently declared holiday' would be those as laid down by Foreign Exchange Dealers' Association of India (FEDAI).

• Expiry date: Also called Last Trading Day, it is the day on which trading ceases in the contract; and is two working days prior to the final settlement date.

• Contract size: The amount of asset that has to be delivered under one contract. Also called as lot size. In the case of USDINR it is USD 1000; EURINR it is EUR 1000; GBPINR it is GBP 1000 and in case of JPYINR it is JPY 100,000.

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4. Initial margin: The amount that must be deposited in the margin account at the time a futures contract is first entered into is known as initial margin.

5. Marking-to-market: In the futures market, at the end of each trading day, the margin account is adjusted to reflect the investor's gain or loss depending upon the futures closing price. This is called marking-to-market.

CASE STUDIES:-

Example 1: An exporter of garments from India has contracted to export 10,000 pieces of shirt to a large retailer in US. The agreed price was USD 100 per shirt and the payment would be made three months after the shipment. The exporter would take one month to manufacture the shirt. The exporter had used the prevailing spot price of 45 as the budgeted price while signing the export contract. To avoid the FX risk, the exporter sells four month futures at the price of 46. The exporter receives USD well on time and he converts USD to INR in the OTC market at the then prevailing price of 47 and also cancels the futures contract at the same time at the price of 47.20. How much was the effective currency price for the exporter.

The effective price would be summation of effect of change in USDINR price on the underlying trade transaction and the effect of change in future price on the currency futures contract.

- Underlying trade transaction: Against the budget of 45, the exporter realizes the price of 47 and therefore there is a net positive change of Rs 2
- Futures contract: Against the contracted price of 46, the exporter had to settle the contract at 47.2 and therefore resulting in a net negative change of Rs 1.2
- Combined effect: The combined effect of change in USDINR spot price and change in future price i.e. (Rs 2) + (- Rs 1.2) = + Rs 0.8
- Effective price: Therefore the effective price was 45 (budgeted price) + 0.8 (effect of hedging and underlying trade transaction) i.e. Rs 45.8.

In the same example, assume that INR appreciated against USD at time of converting USD to INR the spot was 44 and futures contract's cancellation rate was 44.2, the effective currency price for the exporter would still be 45.8. This is because there would be a negative change of Rs 1 on underlying trade transaction and a positive change of Rs 1.8 on futures contract. Therefore the net effect will be summation of – 1 and + 1.8 i.e.Rs 0.8.

Please notice that because of the futures contract exporter always gets a price of 45.8 irrespective of depreciation or appreciation of INR. However, not using currency futures would have resulted in effective rate of 47 (in the first case when INR depreciated from 45 to 47) and effective rate of 44 (in the second case when INR appreciated from 45 to 44). Thus using currency futures, exporter is able to mitigate the risk of currency movement.

2. Let us take an example where an importer hedges only partial amount of total exposure.

This example will also demonstrate the method of computing payoff when hedging is done for partial exposure.

An importer of pulses buys 1000 tons of chickpea at the price of USD1600 per ton. On the day of finalizing the contract, USDINR spot price was 45. The importer was not sure about the INR movement in future but he was more biased towards INR appreciation.

He decides to hedge half of the total exposure using currency futures and contracted a rate of 45.5 for two month contract. In the next two months, INR depreciated to 46.5 at the time of making import payment. Let us assume that the day of making import payment coincides with expiry of future contract and the settlement price of futures contract was declared as 46.7. What was the effective USDINR for the importer and what would it have been had he hedged the full exposure.

The effective price would be summation of final price at which import remittance was made and payoff from the futures contract.

- Futures contract: Against the contracted price of 45.5, the importer settled the contract at 46.7, thereby resulting in a net positive change of Rs 1.2. Since importer hedged only half of the total exposure, the net inflow from hedging would be available for half of total exposure.
- Effective price computation: Therefore the effective price would be 46.5 (final remittance price) for the unhedged part and 45.3 for the balance half which was hedged. The figure of 45.3 is computed by deducting 1.2 (inflow from hedging) from 46.5. Therefore final effective price would be:

(46.5 x 0.5) + (45.3 x 0.5) = 45.9

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Please note that since it is import payment and a lower USDINR exchange rate would be positive for the importer, therefore a positive inflow from future contract is reduced from the remittance price to compute effective price for the hedged part.

As against the effective price of 45.9, the price would have been 45.3 had the importer decided to hedge the total exposure. Also note that without hedging, the effective price would have been 46.5 i.e., the price at which importer made the import remittance.

Did you notice that in the second scenario of full hedging, the effective price (45.3) is different from the contracted price of futures (45.5)? The difference is due to the difference in the final settlement price of futures contract and the price at which remittance was done.

1. Mark to market Case study:

On Monday HLL enters into a future contract of purchasing $1,25,000/- at the rate of $ = Rs.44.50. This contract is to mature on Thursday. At the close of trading on Monday, Tuesday & Wednesday, the future prices are Rs.44.42, 44.65 & 44.22. At the close of trading on Thursday, the spot rate in Rs.44.10. What amount the investor receives / pays on different days? Explain the outcome of the contract explaining the theoretical concepts of the different steps. Initial margin is 1.25% of contrac amount. That means HLL has to deposit = $ 125000 X Rs.44.50 = Rs.55,62,500 X 1.25% = Rs.69,531/- to exchange for this future contract.

The payoff table on mark to market daily basis will be as follows:

Day	Market rate	Strike Price	Gain or loss	Total Gain or loss on contract	Margin Account cash flow
Monday	44.42	44.50	- 0.08	- Rs.10,000	Rs.59,531
Tuesday	44.50	44.50	0.00	0	Rs.59,531
Wednesday	44.65	44.50	0.15	+ Rs.15,000	Rs.74,531
Thursday	44.90	44.50	0.40	+ Rs.40,000	Rs.1,14,531

Here from the above we can conclude that HLL by entering in future contract gained by Rs.15,000+Rs.40,000 – Rs.10,000 = Rs.45,000/-

This can be confirmed :- Margin account bal. Rs.1,14,531 – Initial Margin Rs.69,531
= Rs.45,000/-

- If the rupee will trade at the premium then HLL will suffer a loss as given in following table

Day	Market rate	Strike Price	Gain or loss	Total Gain or loss on contract	Margin Account cash flow
Monday	44.58	44.50	0.08	+ Rs.10,000	Rs.79,531
Tuesday	44.50	44.50	0.00	0	Rs.79,531
Wednesday	44.35	44.50	- 0.15	- Rs.15,000	Rs.64,531
Thursday	44.10	44.50	- 0.40	- Rs.40,000	Rs.24,531

That means HLL lost Rs.45,000/- by entering future contract due to appreciation of rupee.

i) Pricing of Futures Contracts : According to the interest rate parity theory, the currency margin is dependent mainly on the prevailing interest rate (for investment for the given time period) in the two currencies. The forward rate can be calculated by the following formula:

$$\frac{F}{S} = \frac{1+Rh}{1+Rf}$$

Where, F and S are future and spot currency rate. Rh and Rf are simple interest rate in the home and foreign currency respectively. Alternatively, if we consider continuously compounded f interest rate then forward rate can be calculated by using the following formula:

F = S * e (rh – rf)*T

Where rh and rf are the continuously compounded interest rate for the home currency and foreign currency respectively, T is the time to maturity and e = 2.71828 (exponential). If the following relationship between the futures rate and the spot rate does not hold, then there will be an arbitrage opportunity in the market. This will force the futures rate to change so that the relationship holds true.

To explain this, let us assume that one year interest rates in US and India are say 7% and 10% respectively and the spot rate of USD in India is Rs. 44.
From the equation above the one year forward exchange rate should be

AI. = 44 x e(0.10-0.07)*1 = 45.34

Suppose that the one year rate is less than this, say Rs. 44.50. An arbitrageur can:

1. Borrow 1000 USD at 7% per annum for one year and convert to Rs. 44000 and invest the same at 10% (both rates being continuously compounded)
2. An amount of USD 1072.5082 has to be repaid. Buy a forward contract for USD 1072.5082 for Rs. 47726.61 (i.e. Rs. 44.50*1072.5082) USD 1000 converted to Rs. 44000 and invested at 10% pa grows to Rs.52. Of this Rs. 47726.61 shall be used to buy USD 1072.5082 and repay the loan (US Dollars borrowed earlier).

The strategy therefore leaves a risk less profit of Rs. 900.91 2) Currency Option:

As the word suggests, option means a choice or an alternative. To explain the concept though an example, take a case where you want to a buy a house and you finalize the house to be bought. On September 1st 2011, you pay a token amount or a security deposit of Rs 20,000 to the house seller to book the house at a price of Rs 15,00,000 and agree to pay the full amount in three months i.e., on November 30th 2011. After making full payment in three months, you get the ownership right of the house. During these three months, if you decide not to buy the house, because of any reasons, your initial token amount paid to the seller will be retained by him.

In the above example, at the expiry of three months you have the option of buying or not buying the house and house seller is under obligation to sell it to you. In case during
these three months the house prices drop, you may decide not to buy the house and lose the initial token amount. Similarly if the price of the house rises, you would certainly buy the house. Therefore by paying the initial token amount, you are getting a choice/ option to buy or not to buy the house after three months.
The above arrangement between house buyer and house seller is called as option contract. We could define option contract as below:

Option: It is a contract between two parties to buy or sell a given amount of asset at a pre- specified price on or before a given date.

We will now use the above example, to define certain important terms relating to options.

- The right to buy the asset is called call option and the right to sell the asset is called put option.
- The pre-specified price is called as strike price and the date at which strike price is applicable is called expiration date.
- The difference between the date of entering into the contract and the expiration date is called time to maturity.
- The party which buys the rights but not obligation and pays premium for buying the right is called as option buyer and the party which sells the right and receives premium for assuming such obligation is called option seller/ writer.
- The price which option buyer pays to option seller to acquire the right is called as option price or option premium
- The asset which is bought or sold is also called as an underlying or underlying asset.

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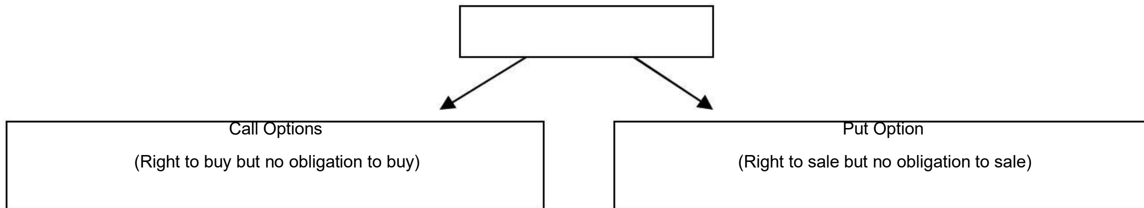
Buying an option is also called as taking a long position in an option contract and selling is also referred to as taking a short position in an option contract.

There are two types of Currency options i.e CALL & PUT as elucidated below.



For example, a ABC Ltd having a liability in Euro with a view that the Euro/USD rate will be higher on maturity date will buy an Euro call. On the maturity date, he has the option to buy the Euro at the strike price or buy it from the market in case it is cheaper. If the ABC Ltd buys a Call Option with a strike price at 0.9000 and on maturity date, the rate is 0.8700, the ABC Ltd has the right to exercise the option. Since in the example cited, it would be cheaper for the ABC Ltd to by the Euro from the market, the ABC Ltd -will not exercise the option

Style of options

Based on when the buyer is allowed to exercise the option, options are classified into two types:

A. European options: European options can be exercised by the buyer of the option only on the expiration date. In India, all the currency options in OTC market are of European type.

B. American options: American options can be exercised by the buyer any time on or before the expiration date. Currently American options are not allowed in currencies in India.

Illustration:-

Purchased Call option: Corporate buys a USD call option for covering its import transactions from a ABN AMRO bank on 1 June 2011, at a strike rate of 45.50. The expiry date is 3 months i.e. 31st August 2011. The premium is 30 paise on the call. Gain or loss at various levels of exchange rate are demonstrated below vide pay off table

Market Rate	Exercise Rate call @ 45.50	Premium paid	Gain/Loss
43.00	0.00	0.30	-0.30
43.50	0.00	0.30	-0.30
44.00	0.00	0.30	-0.30
44.50	0.00	0.30	-0.30
46.00	0.50	0.30	0.20
46.50	1.00	0.30	0.70

When spot exchange rate rises above the strike price, there are gains, when it falls below the strike price there are losses, which are maximum to the extent of premium paid.

That means it is always advisable to exercise Call Option when the spot rate is more and strike price is lower.

Illustration:-

Buying Put Option : A leading garment exporter sold Put option in which USD shall be purchased at 45.50, Premium paid for buying put option is 30 paise. Gain or loss at various levels of exchange rate are shown above vide pay off table is given below.

Market Exercise Rate @ 45.50 Premium paid Gain/Loss Rate

44.00	1.00	0.30	0.70
45.00	- 0.50	0.30	0.30
46.00	0.00	0.30	0.30
46.50	0.00	0.30	0.30
47.00	0.00	0.30	0.30

When spot exchange rate rises above the strike price, the put option will not give any profit but when it falls below the strike price there are profits.
That means it is always advisable to exercise Put Option when the spot rate is less and strike price is higher.

Selling Put Option : A leading garment exporter sold Put option in which USD shall be purchased at 45.50, Premium paid for buying put option is 30 paise. Gain or loss at various levels of exchange

rate are shown above vide pay off table is given below.

Market Rate	Exercise Rate selling put @ 45.50	Premium Received	Gain/Loss
45.00	- 0.50	0.30	- 0.20
46.00	0.00	0.30	0.30
46.50	0.00	0.30	0.30
47.00	0.00	0.30	0.30
	0.00		0.30

When spot exchange rate rises above the strike price, there are gains, when it falls below the strike price there are losses, which are maximum to the extent of premium received.
That means it is always advisable to exercise Put Option when the spot rate is more and strike price is lower.

From above three illustrations one must conclude that the strategy will depend on the following factors:

1. Who is a party to options i.e Importer or Exporter
2. Perception of exchange rate movement i.e At premium or at Discount
3. Premium to paid/received

What is meant by the terminology that an option is in the money, at the money, or out-of-the-money?

Answer: A call (put) option with St > E (E > St) is referred to as trading in-the-money.

If St ≅ E the option is trading at-the-money.

If St < E (E < St) the call (put) option is trading out-of-the money.

St = Strike Price
E = Exercise Price

CASE STUDIES:-

1. An American manufacturer ABC plc. Ltd purchases Japanese goods worth 90 million Yens, credit terms 1 month. i.e. the manufacturer has to pay ,after one month, the Japanese company 90 million Yen no matter what happens to the Yen-Dollar rate. That means the American co. is at risk if the rate is not favorable. Here ABC plc. Ltd can hedge this risk by entering into option contract. The co can buy a foreign currency option which gives him the right but not the obligation to buy 90 million yen at 110 Yens per Dollar. The option carries a premium or cost of US $ 0.02 million. Now there can be Three Possibilities as regards this call option:-

a. If Yen Falls: Say 120 yens per US $ then ABC plc. Ltd will purchase Yens from the

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market instead of going for option as he will need to pay only 0.75 million US $ to spot market. The Co. will benefit even if they lost the premium on call option.

b. If Yen is Stable: ABC plc. Ltd purchases 90 million Yens either from the market or under his option. He has to pay US $ 1.0909 million. Cost is $0.02 million, i.e. premium for purchasing option.

c. If Yen Rises or will be at premium: Suppose after three months, yen rises to 100 Yen per US $. If ABC plc. Ltd purchases Yens from the market, he has to pay 90 million / 100. i.e., 0.90 million US $. That means co. can purchase yen by paying $ 9,00,000.

Whereas if Co. exercises the option, he can purchase 90 million Yens for at 110 yens per dollar or 90million/110 i.e 0.818 million US $. Or co. can purchase yen by paying $ 8,18,182. That means a savings of $ 81818.00 over spot market.

And therefore Co. should exercise the option as the Net saving is $ 81,818 – Premium paid $20,000 = $ 61,818

2. An American firm has just bought merchandise from a British firm for £50,000 on terms of net 90 days. The U.S. company has purchased a 3-month call option of 50,000 pounds at a strike of $1.7 per pound and premium cost of $0.02 per pound. On the day the option matures, the spot exchange rate is $1.8 per pound. Should the U.S. company exercise the option at that time or buy British pounds in the spot market?

A. exercise the option
B. buys British pound spot
C. does not make any difference
D. cannot tell
E. none of the above

Answer:- A… Explanation for answer:-

Here since American Firm is an importer and therefore need pounds to be delivered. Hence will go for call option for to hedge position of purchase of £.

The contract in $ terms will be
Call option = £50,000 x $1.7 = $85,000, that means in this option the American firm can get £50,000 by giving $85000.

Now since this contract is of 3 months, on the maturity the American firm has decide what to do with this contract either to exercise or leave it. If the rate favours the American firm then they will go with exercising the option under the contract. That means they will purchase the £ by giving $.

On maturity the spot rate is $1.8 which means if the American Firm not exercised the call option they need to have spend in Spot transaction = £50,000 x $1.8 = $90,000.

Here, it is now very much clear that Spot transaction is not beneficial to firm and hence, the U.S. company should exercise the call option which will save $5,000 over the spot transaction.

BI. An American firm has just bought merchandise from a British firm for £50,000 on terms of net 90 days. The U.S. company has purchased a 3-month call option on 50,000 pounds at a strike price of $1.7 per pound and a premium cost of $0.02 per pound. On the day the option matures, the spot exchange rate is $1.8 per pound. What will be the approximate value of the pound payable in U.S. dollars if the U.S. company exercises the option at that time?

$91,000B. $90,000 C.$86,000 D. $85,000 E. $81,000

o Assume that on 1st December 2011, USD-INR spot was at 45, premium for January 2012 maturity put option at strike of 45.5 is INR 0.54/0.55 and premium for January 2011 maturity call

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option at strike of 45 is INR 0.71/0.72. A client executes a trade wherein, client has entered sales put (i.e he will be put writer) at a strike of 45.5 and a call at a strike of 45. On expiry the RBI reference rate is 46.07. How much net profit/loss did the client make per USD?

(a) Loss of INR 0.2 (b) Profit of INR 0.15 (c) Profit of INR 0.91 (d) Loss of INR 0.96

Answer:- (c) …. Sale Put at strike price of Rs.45.5 and he must have received premium of Rs.0.55.
Call at Strike price of Rs.45.00 and he must have paid premium of Rs.0.71.

Now rate at the maturity is Rs.46.07, here the put buyer will not exercise the put option at strike price of Rs.45.50 (as the strike price is lower than RBI reference rate) and therefore the client as put writer will retain the premium.

However since he has in the money for call option (strike price is less than reference rate) he will benefit as 46.07 – 45 = 1.07

Now, Net payoff on this option strategy is = Rs.1.07 + 0.55- 0.71 = Profit of Rs.0.91

- Assume today's closing price on a NSE futures contract is $0.9716/EUR. You have a short (future sale) position in one contract with strike price today's closing. Your margin account currently has a balance of $1,700. The next three days' settlement prices are $ 0.9702, $0.9709, and $0.9762. Calculate the changes in the margin account from daily marking -to-market and the balance of the margin account after the third day. Contract of € 1,25,000.

Solution:
$1,700 + [($0.9716 – $0.9702) + ($0.9716 – $0.9709) + ($0.9716 – $0.9722)] x €125,000 = Or $ 1,700 + [$0.0014 + $0.0007 - $0.0006] X €
125000
= $1,887.50.

- Mr. Martin enters into one contract of purchasing futures of GBP on January 27, 2011 at a price of £ = 1.50 USD. The standard size of one future contract is £1,00,000. Using rates of £ = $ on different date: find gain /loss of Mr. Martin at this closing of each of above mentioned dates.
January 27 $ 1.38, January 28 $ 1.56, January 29 $ 1.63, January 30 $ 1.28, January 31 $ 1.81.

If the initial margin if $ 5,000 per contract and maintenance margin is $ 3,000 per contract, show Mr. Martin's margin account (also called as equity account) and the additional deposits to be made (assume no withdrawals).

Date	Market rate	Difference = strike &	Adjustment in margin + / -		Additional Deposit required above $ 8000
27.01	1.38	- 0.12	100000 x -0.12 = $	-12,000	$ 4,000
28.01	1.56	+ 0.06	100000 x 0.06 = $	6,000	0
29.01	1.63	+ 0.13	100000 x 0.13 = $	13,000	0
30.01	1.28	- 0.22	100000 x -0.22 = $	- 22,000	$ 10,000
		+ 0.31			

- A Singapore based firm exported goods to an Australian firm, invoice Australian dollars 4,00,000 on 2nd April, 2011, the payment is due on 25thJune 2011. On 18thApril, 2011, the finance manager of the Singapore firm got an indication that the Singapore Dollar (SGD) will appreciate against Australian Dollar (AUD). The following foreign exchange rates are quoted on 18th April, 2011 : Spot SGD/AD = 1.4760 & Dec. 2011 futures contract SGD/AUD = 1.4835. The standard size of the futures contract is AUD 1,00,000.

a. Suggest the hedging Strategy? Assuming that the finance manager follows your suggestion, find net cash inflow on 25th June, 2011 assuming that on that day the following rates were prevailed in the market:
Spot SGD/AUD = 1.4275 Dec. 2007 futures contract SGD/AUD = 1.3998.

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b. In Singapore, the forward price on SGD for delivery in 60 days is quoted at 1.60 per USD. The futures market price for a similar contract is 0.65. Is there some arbitrage opportunity?

Answer:-

a. For hedging a firm need to buy future sale contract at a strike price of SGD = 1.4845.

The pay off at the date of cash flow i.e 25th June,2011, will be as follows:

4 contracts of AUD 1,00,000 will have to be entered.

Now on 25th June the strike 1.4845 and spot is 1.4275 and hence we will gain 1.4845 – 1.4275 = AUD 0.057 x 4,00,000 = AUD 22,800.

So there is profit in going with futures.

b. Forward price: 1 $ = 1.60SGD.

Future prices are in indirect quotations. Hence direct quote for future price:

1SGD = 0.65$ means

1 / $0.65

= 1$ = 1.5385 SGD

Arbitrage opportunity is there. Buy $ in futures market @ 1.5385 SGD.

1. Mihan Ltd has purchased a 3-months call option of € with an exercise price of Rs.71. Determine the value of Call option at expiration if the Euro price at expiration turns out to be either 67 or 74. Answer:

Spot price on maturityValue call option

670

74Rs.3

9. A London based firm has supplied a heavy machine to a New–York based firm for $10 million, payment due in 4 months time. The current spot rate is 1£ = $ 1.58. The London firm has apprehensions that USD may decline against British Pound. The London firm is considering the proposal of buying a put option, 4 months maturity, strike Price: 1£ = $ 1.60. The option premium is $0.0002 per £. Explain the position of the London firm on maturity at $ 1.59.

Put Strike $1.60, maturity $1.59 and hence London company will loose £ = $0.01

OR The ultimate effect on company:

At strike price = $ 10 million x 0.01 = $1,00,000

From the above it can be seen that company will lose around $1,00,000 if they go with put and hence they will not exercise put option and there maximum loss will be premium $ 2,000 on $ 10 million put contract.

o A US importer has decided to buy German goods worth € 105,000 and must settle the account in a month's time. At the moment, the spot exchange rate is US $0.7284/€. He runs the risk that the euro will appreciate against the dollar, pushing up his dollar costs. One solution would be to buy a euro contract on the CME (each contract is worth €125,000) at the futures rate of US $ 0.7458. In a month's time, the spot rate might move to US $0.7444 and the futures price to US $0.7430. If he chose to go ahead with future what will be gain or loss:

Answer:

So the rise in the cost of the goods would be (US $0.7444 – US $0.7284) x €125,000 = US $2,000 if not going ahead with futures.

However, he can close out the futures position at a profit of US $ 350: (US $0.7458 – US $0.7430) x €125,000.

Thus, despite the fact that the contract size exactly matched his exposure, the hedger still actually lost out slightly. This is because the cash and futures markets did not move exactly in tandem. If rates had not moved in his favour, the exporter would have lost money on the futures position but gained on the post transaction.

The short hedge would work in the same way. An exporter contracted to sell US goods for a fixed sum in deutschmarks runs the risk that the deutschmark will decline against the dollar. He would sell the appropriate number of contracts to hedge this risk.

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o An IT professional buys a house for INR 500,000 for which payment has to be made after three months. As he is expecting to receive USD 10,000 in three months, he executes 10 USDINR futures contracts to hedge currency risk at a price of 50. When he received the payment, he converted USD into INR with his bank at a price of 51 for making the payment for the house and also settles the contract at a price of 49. Given this situation, would he have sold/ bought USDINR futures and would the effective price for house be lower than or higher than USD 10,000?

(a) Bought, Higher (b) Sold, Higher (c) Bought, Lower (d) Sold, Lower

p A trader executes following currency futures trade: buys one lot of USD/INR, sells one lot of JPY/INR. What view has he executed?

(a) JPY strengthening against USD (b) JPY weakening against USD (c) INR strengthening against USD (d) INR weakening against JPY

Unsloved:

Q:1 One year interest rates in US and India are say 7% and 10% respectively and the spot rate of USD in India is Rs. 47. One year forward exchange rate should be Rs. ____.

(a) 48.78 (b) 48.43 (c) 47.45 (d) 47.86

Q:2 One year interest rates in US and India are say 7% and 11% respectively and the spot rate of USD in India is Rs. 38. One year forward exchange rate should be Rs. ____.

(a) 39.55 (b) 39.90 (c) 40.67 (d) 40.56

Q:3 An oil -importing firm - ABC Co. is expected to make future payments of USD 100000 after 3 months (in USD) for payment against oil imports. Suppose the current 3-month futures rate is Rs. 60. ABC Co. can go ____ in the futures contract to hedge itself.

(a) Short

(b) Long

Q:4 A speculator buys 107 USD-INR contracts @ Rs. 49.00 per contract and sells them @ Rs. 50.00 per contract. Assuming 1 contract = 1000 USD, the total profit made by the speculator is Rs. ______

(a) 107000 (b) 109000 (c) 1070 (d) 10700

Q:5 A speculator buys 65 USD-INR contracts @ Rs. 41.00 per contract and sells them @ Rs. 42.00 per contract. Assuming 1 contract = 1000 USD, the speculator ends up with a _____.

(a) loss (b) profit (c) no profit no loss

Q:6 A speculator sells 65 USD-INR contracts @ Rs. 41.00 per contract and buys them @ Rs. 40.00 per contract. Assuming 1 contract = 1000 USD, the speculator ends up with a _____.

(a) loss (b) profit (c) no profit no loss

Q.7 A person has invested USD 100,000 in US equities with a view of appreciation of US stock market. In next one year, his investments in US equities appreciated in value to USD120,000. The investor decided to sell off his portfolio and repatriate the capital and profits to India. At the time of investing abroad the exchange rate was 44.5 and at the time of converting USD back into INR, he received an exchange rate of 46. How much is the return on investment in USD and in INR respectively?

(a) 20%, 16% (b) 20%, 24% (c) 20%, 20% (d) 20%, 18%

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CHAPTER 3
LC & UPCDC 600

Introduction
Letter of Credit L/c also known as Documentary Credit is a widely used term to make payment secure in domestic and international trade. The document is issued by a financial organization at the buyer request. Buyer also provide the necessary instructions in preparing the document.
The International Chamber of Commerce (ICC) in the Uniform Custom and Practice for Documentary Credit (UCPDC) defines L/C as:
"An arrangement, however named or described, whereby a bank (the Issuing bank) acting at the request and on the instructions of a customer (the Applicant) or on its own behalf :

1. Is to make a payment to or to the order third party (the beneficiary) or is to accept bills of exchange (drafts) drawn by the beneficiary.
2. Authorised another bank to effect such payments or to accept and pay such bills of exchange (draft).
3. Authorised another bank to negotiate against stipulated documents provided that the terms are complied with.

A key principle underlying letter of credit (L/C) is that banks deal only in documents and not in goods. The decision to pay under a letter of credit will be based entirely on whether the documents presented to the bank appear on their face to be in accordance with the terms and conditions of the letter of credit.
Parties to Letters of Credit

- Applicant (Opener): Applicant which is also referred to as account party is normally a buyer or customer of the goods, who has to make payment to beneficiary. LC is initiated and issued at his request and on the basis of his instructions.
- Issuing Bank (Opening Bank) : The issuing bank is the one which create a letter of credit and takes the responsibility to make the payments on receipt of the documents from the beneficiary or through their banker. The payments has to be made to the beneficiary within seven working days from the date of receipt of documents at their end, provided the documents are in accordance with the terms and conditions of the letter of credit. If the documents are discrepant one, the rejection thereof to be communicated within seven working days from the date of of receipt of documents at their end.
- Beneficiary : Beneficiary is normally stands for a seller of the goods, who has to receive payment from the applicant. A credit is issued in his favour to enable him or his agent to obtain payment on surrender of stipulated document and comply with the term and conditions of the L/c.
- If L/c is a transferable one and he transfers the credit to another party, then he is referred to as the first or original beneficiary.
- Advising Bank : An Advising Bank provides advice to the beneficiary and takes the responsibility for sending the documents to the issuing bank and is normally located in the country of the beneficiary.
- Confirming Bank : Confirming bank adds its guarantee to the credit opened by another bank, thereby undertaking the responsibility of payment/negotiation acceptance under the credit, in additional to that of the issuing bank. Confirming bank play an important role where the exporter is not satisfied with the undertaking of only the issuing bank.
- Negotiating Bank: The Negotiating Bank is the bank who negotiates the documents submitted to them by the beneficiary under the credit either advised through them or restricted to them for negotiation. On negotiation of the documents they will claim the reimbursement under the credit and makes the payment to the beneficiary provided the documents submitted are in accordance with the terms and conditions of the letters of credit.
- Reimbursing Bank : Reimbursing Bank is the bank authorized to honor the reimbursement claim in settlement of negotiation/acceptance/payment lodged with it by the negotiating bank. It is normally the bank with which issuing bank has an account from which payment has to be made.

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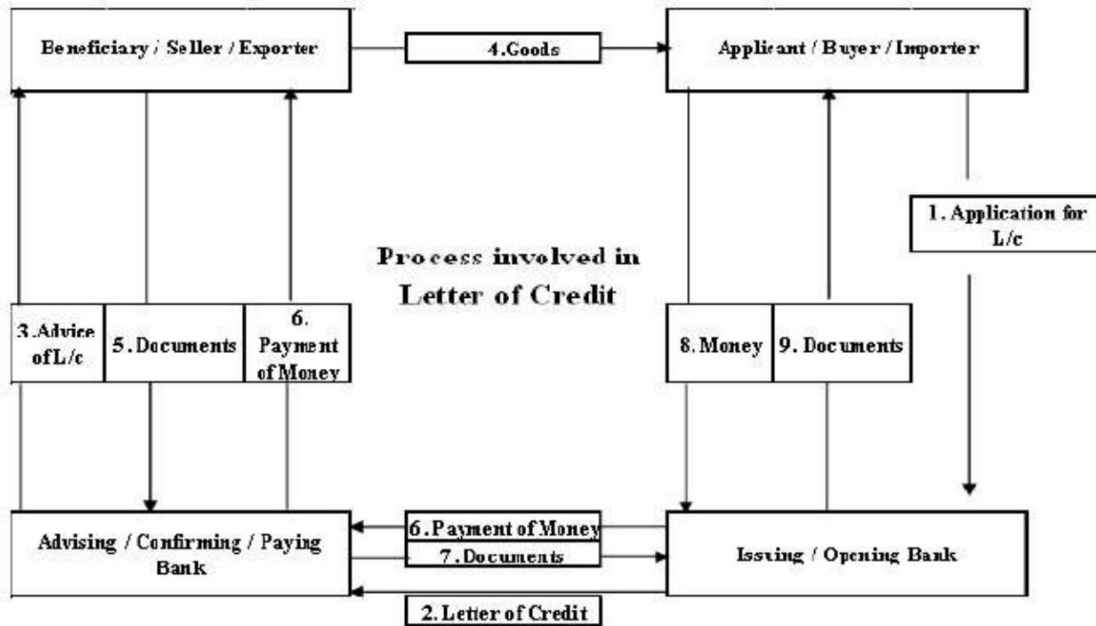
- Second Beneficiary : Second Beneficiary is the person who represent the first or original Beneficiary of credit in his absence. In this case, the credits belonging to the original beneficiary is transferable. The rights of the transferee are subject to terms of transfer.

Process involved in Letter of Credits.



The following is a step-by-step description of a typical Letter of Credit transaction:

1. An Importer (Buyer) and Exporter (Seller) agree on a purchase and sale of goods where payment is made by Letter of Credit.

2. The Importer completes an application requesting its bank (Issuing Bank) to issue a Letter of Credit in favor of the Exporter. Note that the Importer must have a line of credit with the Issuing Bank in order to request that a Letter of Credit be issued.

3. The Issuing Bank issues the Letter of Credit and sends it to the Advising Bank by telecommunication or registered mail in accordance with the Importer's instructions. A request may be included for the Advising Bank to add its confirmation. The Advising Bank is typically located in the country where the Exporter carries on business and may be the Exporter's bank but it does not have to be.

4. The Advising Bank will verify the Letter of Credit for authenticity and send a copy to the Exporter.

5. The Exporter examines the Letter of Credit to ensure:
a. It corresponds to the terms and conditions in the purchase and sale agreement; b. Documents stipulated in the Letter of Credit can be produced; and c. The terms and conditions of the Letter of Credit may be fulfilled.

6. If the Exporter is unable to comply with any term or condition of the Letter of Credit or if the Letter of Credit differs from the purchase and sale agreement, the Exporter should immediately notify the Importer and request an amendment to the Letter of Credit.

o When all parties agree to the amendments, they are incorporated into the terms of the Letter of Credit and advised to the Exporter through the Advising Bank. It is recommended that the Exporter does not make any shipments against the Letter of Credit until the required amendments have been received.

p The Exporter arranges for shipment of the goods, prepares and/or obtains the documents specified in the Letter of Credit and makes demand under the Letter of Credit by presenting the documents within the stated period and before the expiry date to the "available with" Bank. This may be the Advising/Confirming Bank. That bank checks the documents against the Letter of Credit and forwards them to the Issuing Bank. The drawing is negotiated, paid or accepted as the case may be.

q The Issuing Bank examines the documents to ensure they comply with the Letter of Credit terms and conditions. The Issuing Bank obtains payment from the Importer for payment already made to the "available with" or the Confirming Bank.

r Documents are delivered to the Importer to allow them to take possession of the goods from the transport company. The trade cycle is complete as the Importer has received its goods and the Exporter has obtained payment.

Types of Letter of Credit :

1. Revocable Letter of Credit L/c

A revocable letter of credit may be revoked or modified for any reason, at any time by the issuing bank without notification. It is rarely used in international trade and not considered satisfactory for the exporters but has an advantage over that of the importers and the issuing bank.

There is no provision for confirming revocable credits as per terms of UCPDC, Hence they cannot be confirmed. It should be indicated in LC that the credit is revocable. if there is no such indication the credit will be deemed as irrevocable.

2. Irrevocable Letter of CreditL/c

In this case it is not possible to revoked or amended a credit without the agreement of the issuing bank, the confirming bank, and the beneficiary. Form an exporters point of view it is believed to be more beneficial. An irrevocable letter of credit from the issuing bank insures the beneficiary that if the required documents are presented and the terms and conditions are complied with, payment will be made.

3. Confirmed Letter of Credit L/c

Confirmed Letter of Credit is a special type of L/c in which another bank apart from the issuing bank has added its guarantee. Although, the cost of confirming by two banks makes it costlier, this type of L/c is more beneficial for the beneficiary as it doubles the guarantee.

4. Sight Credit and Usance Credit L/c

Sight credit states that the payments would be made by the issuing bank at sight, on demand or on presentation. In case of usance credit, draft are drawn on the issuing bank or the correspondent bank at specified usance period. The credit will indicate whether the usance draft are to be drawn on the issuing bank or in the case of confirmed credit on the confirming bank.

5. Back to Back Letter of Credit L/c

Back to Back Letter of Credit is also termed as Countervailing Credit. A credit is known as backtoback credit when a L/c is opened with security of another L/c.

A backtoback credit which can also be referred as credit and countercredit is actually a method of financing both sides of a transaction in which a middleman buys goods from one customer and sells them to another.

The parties to a BacktoBack Letter of Credit are:

1.The buyer and his bank as the issuer of the original Letter of Credit.

2. The seller/manufacturer and his bank,

3. The manufacturer's subcontractor and his bank.

The practical use of this Credit is seen when L/c is opened by the ultimate buyer in favour of a particular beneficiary, who may not be the actual supplier/ manufacturer offering the main credit

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with near identical terms in favour as security and will be able to obtain reimbursement by presenting the documents received under back to back credit under the main L/c.

The need for such credits arise mainly when:

1. The ultimate buyer not ready for a transferable credit
2. The Beneficiary do not want to disclose the source of supply to the openers.
3. The manufacturer demands on payment against documents for goods but the beneficiary of credit is short of the funds

6. Transferable Letter of Credit L/c

A transferable documentary credit is a type of credit under which the first beneficiary which is usually a middleman may request the nominated bank to transfer credit in whole or in part to the second beneficiary.

The L/c does state clearly mentions the margins of the first beneficiary and unless it is specified the L/c cannot be treated as transferable. It can only be used when the company is selling the product of a third party and the proper care has to be taken about the exit policy for the money transactions that take place.

This type of L/c is used in the companies that act as a middle man during the transaction but don't have large limit. In the transferable L/c there is a right to substitute the invoice and the whole value can be transferred to a second beneficiary.

The first beneficiary or middleman has rights to change the following terms and conditions of the letter of credit:

1. Reduce the amount of the credit.
2. Reduce unit price if it is stated
3. Make shorter the expiry date of the letter of credit.
4. Make shorter the last date for presentation of documents.
5. Make shorter the period for shipment of goods.
6. Increase the amount of the cover or percentage for which insurance cover must be effected.
7. Substitute the name of the applicant (the middleman) for that of the first beneficiary (the buyer).

Standby Letter of Credit L/c

Initially used by the banks in the United States, the standby letter of credit is very much similar in nature to a bank guarantee. The main objective of issuing such a credit is to secure bank loans. Standby credits are usually issued by the applicant's bank in the applicant's country and advised to the beneficiary by a bank in the beneficiary's country.

Unlike a traditional letter of credit where the beneficiary obtains payment against documents evidencing performance, the standby letter of credit allow a beneficiary to obtains payment from a bank even when the applicant for the credit has failed to perform as per bond.

A standby letter of credit is subject to "Uniform Customs and Practice for Documentary Credit" (UCP), International Chamber of Commerce Publication No 500, 1993 Revision, or "International Standby Practices" (ISP), International Chamber of Commerce Publication No 590, 1998.

"Red Clause" LC :-

In the case of a red clause letter of credit (documentary credit with advance payment) the seller can request that the correspondent bank pay an agreed amount in advance (defined in the terms and conditions of the documentary credit) . The advance is basically intended to finance the production or purchase of the goods to be delivered under the documentary credit. The advance is normally paid against receipt and commitment in writing from the beneficiary to subsequently deliver the transportation documents by an agreed date.

IF in the LC this clause is permitted then it will be printed in RED INK.

"Green Clause"

In the case of a green clause letter of credit (documentary credit with advance payment) the beneficiary can request that the correspondent bank pay an agreed amount in advance (defined in the terms and conditions of the letter of credit). The advance is basically intended to finance the production or purchase of the goods to be delivered under the documentary credit. Unlike the red

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clause letter of credit, the advance is paid only against receipt of an additional document providing proof that the goods to be shipped have been warehoused, as well as against receipt and written commitment from the beneficiary to subsequently deliver the transportation documents by an agreed date.
IF in the LC this clause is permitted then it will be printed in GREEN INK.

Amendments to a Letter of Credit:
After issuance of a Letter of Credit, changes can be done through amendments subject to acceptance by the Exporter. Amendments to the Letter of Credit will be required when either the Importer or the Exporter is unable to comply with the terms of the sale agreement or the agreement has been changed. For example, an Exporter will ask for an amendment to extend the expiry date and the latest shipping date if they are unable to manufacture the merchandise according to the agreed upon time. An Importer may request an amendment to increase the value of the Letter of Credit if they subsequently decide to purchase a higher quantity of merchandise. The Importer must complete an amendment application listing all required changes and forward the request to the respective Global Trade Finance office via the same route the original application was sent. Amendment requests will be processed subject to credit approval by the Issuing Bank where necessary. Any amendments to the Letter of Credit must be accepted by the Exporter and where more than one change is included in an amendment, they must be accepted as a whole as opposed to accepting or rejecting individual items within the amendment.
Import Operations Under L/c
The Import Letter of Credit guarantees an exporter payment for goods or services, provided the terms of the letter of credit have been met.
A bank issue an import letter of credit on the behalf of an importer or buyer under the following Circumstances

- When a importer is importing goods within its own country.
- When a trader is buying good from his own country and sell it to the another country for the purpose of merchandizing trade.
- When an Indian exporter who is executing a contract outside his own country requires importing goods from a third country to the country where he is executing the contract.

The first category of the most common in the day to day banking

Fees And Reimbursements
The different charges/fees payable under import L/c is briefly as follows
The issuing bank charges the applicant fees for opening the letter of credit. The fee charged depends on the credit of the applicant, and primarily comprises of :
(a) Opening Charges This would comprise commitment charges and usance charged to be charged upfront for the period of the L/c.
The fee charged by the L/c opening bank during the commitment period is referred to as commitment fees. Commitment period is the period from the opening of the letter of credit until the last date of negotiation of documents under the L/c or the expiry of the L/c, whichever is later.
Usance is the credit period agreed between the buyer and the seller under the letter of credit. This may vary from 7 days usance (sight) to 90/180 days. The fee charged by bank for the usance period is referred to as usance charges.
(b)Retirement Charges

1. This would be payable at the time of retirement of LCs. LC opening bank scrutinizes the bills under the LCs according to UCPDC guidelines , and levies charges based on value of goods.
2. The advising bank charges an advising fee to the beneficiary unless stated otherwise The fees could vary depending on the country of the beneficiary. The advising bank charges may be eventually borne by the issuing bank or reimbursed from the applicant.
3. The applicant is bounded and liable to indemnify banks against all obligations and responsibilities imposed by foreign laws and usage.

- o The confirming bank's fee depends on the credit of the issuing bank and would be borne by the beneficiary or the issuing bank (applicant eventually) depending on the terms of contract.
- p The reimbursing bank charges are to the account of the issuing bank.

Risk associated with Opening Imports L/c's

The basic risk associated with an issuing bank while opening an import L/c are :

1. The financial standing of the importer

   As the bank is responsible to pay the money on the behalf of the importer, thereby the bank should make sure that it has the proper funds to pay.

2. The goods

   Bankers need to do a detail analysis against the risks associated with perishability of the goods, possible obsolescence, import regulations packing and storage, etc. Price risk is the another crucial factor associated with all modes of international trade.

   There is always the risk of exporting inferior quality goods. Banks need to be protective by finding out as much possible about the exporter using status report and other confidential information.

   These types of risks are mainly associated with the political and economic scenario of a country. To solve this issue, most banks have specialized unit which control the level of exposure that that the bank will assumes for each country.

5. Foreign exchange risk

   Foreign exchange risk is another most sensitive risk associated with the banks. As the transaction is done in foreign currency, the traders depend a lot on exchange rate fluctuations.

Export operations under L/c

Export Letter of Credit is issued in for a trader for his native country for the purchase of goods and services. Such letters of credit may be received for following purpose:

1. For physical export of goods and services from India to a Foreign Country.
2. For execution of projects outside India by Indian exporters by supply of goods and services from Indian or partly from India and partly from outside India.
3. Towards deemed exports where there is no physical movements of goods from outside India But the supplies are being made to a project financed in foreign exchange by multilateral agencies, organization or project being executed in India with the aid of external agencies.
4. For sale of goods by Indian exporters with total procurement and supply from outside India. In all the above cases there would be earning of Foreign Exchange or conservation of Foreign Exchange.

Banks in India associated themselves with the export letters of credit in various capacities such as advising bank, confirming bank, transferring bank and reimbursing bank.

In every case the bank will be rendering services not only to the Issuing Bank as its agent correspondent bank but also to the exporter in advising and financing his export activity.

The basic responsibility of an advising bank is to advise the credit received from its overseas branch after checking the apparent genuineness of the credit recognized by the issuing bank.

It is also necessary for the advising bank to go through the letter of credit, try to understand the underlying transaction, terms and conditions of the credit and advice the beneficiary in the matter.

The main features of advising export LCs are:

1. There are no credit risks as the bank receives a onetime commission for the advising service.
2. There are no capital adequacy needs for the advising function.

Advising of Amendments to L/Cs

Amendment of LCs is done for various reasons and it is necessary to fallow all the necessary the procedures outlined for advising. In the process of advising the amendments the Issuing bank serializes the amendment number and also ensures that no previous amendment is missing from the list. Only on receipt of satisfactory information/ clarification the amendment may be advised.

3. Confirmation of Export Letters of Credit

It constitutes a definite undertaking of the confirming bank, in addition to that of the issuing bank, which undertakes the sight payment, deferred payment, acceptance or negotiation. Banks in India have the facility of covering the credit confirmation risks with ECGC under their "Transfer Guarantee" scheme and include both the commercial and political risk involved.

4. Discounting/Negotiation of Export LCs

When the exporter requires funds before due date then he can discount or negotiate the LCs with the negotiating bank. Once the issuing bank nominates the negotiating bank, it can take the credit risk on the issuing bank or confirming bank.

However, in such a situation, the negotiating bank bears the risk associated with the document that sometimes arises when the issuing bank discover discrepancies in the documents and refuses to honor its commitment on the due date.

5. Reimbursement of Export LCs

Sometimes reimbursing bank, on the recommendation of issuing bank allows the negotiating bank to collect the money from the reimbursing bank once the goods have been shipped. It is quite similar to a cheque facility provided by a bank.

In return, the reimbursement bank earns a commission per transaction and enjoys float income without getting involve in the checking the transaction documents.

Reimbursement bank play an important role in payment on the due date (for usance LCs) or the days on which the negotiating bank demands the same (for sight LCs).

Opening of imports LCs in India involve compliance of the following main regulation:

i.Trade Control Requirements

The movement of good in India is guided by a predefined se of rules and regulation. So, the banker needs to assure that make certain is whether the goods concerned can be physically brought in to India or not as per the current EXIM policy.

ii.Exchange Control Requirements

The main objective of a bank to open an Import LC is to effect settlement of payment due by the Indian importer to the overseas supplier, so opening of LC automatically comes under the policies of exchange control regulations.

UCPDC Guidelines

Uniform Customs and Practice for Documentary Credit (UCPDC) is a set of predefined rules established by the International Chamber of Commerce (ICC) on Letters of Credit. The UCPDC is used by bankers and commercial parties in more than 200 countries including India to facilitate trade and payment through LC.

UCPDC was first published in 1933 and subsequently updating it throughout the years. In 1994, UCPDC 500 was released with only 7 chapters containing in all 49 articles. .

The latest revision was approved by the Banking Commission of the ICC at its meeting in Paris on 25 October 2006. This latest version, called the UCPDC600, formally commenced on 1 July 2007. It contains a total of about 39 articles covering the following areas, which can be classified as 8 sections according to their functions and operational procedures.

	Article	Area	Consisting
1.	1 to 3	General	Application, Definition and Interpretations
	4 to 12		

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			vs. Goods
3.	13 to 16	Liabilities and responsibilities.	Reimbursement, Examination of Documents, Complying, Presentation, Handling Discrepant Documents
4.	17 to 28	Documents	Bill of Lading, Chapter Party Bill of Lading, Air Documents, Road Rail etc. Documents, Courier , Postal etc. Receipt. On board, Shippers' count, Clean Documents, Insurance documents Extension of dates, Tolerance in Credits, Partial Shipment and Drawings. House of Presentation
5.	29 to 33	Miscellaneous Provisions	Effectiveness of Document Transmission and Translation Force Majeure
6	34 to 37	Disclaimer	
7	38 & 39	Others	Transferable Credits Assignment of Proceeds

CASE STUDY:

I. A LC has mentioned that as per Article 20 (UPCDC 600) indication of port of loading, port of discharge, and that the goods have been loaded on board 'a named vessel' is required while negotiating the LC. When documents came for negotiation, the Bill of lading evidencing Bangkok as the port of loading with addition of the words "via Singapore" to indicate that there will be a transshipment in Singapore, Rotterdam as the port of discharge, "vessel Y" as the ocean vessel. Negotiating bank refused to accept the documents and returned by mentioning reason a bill of lading is required covering a port to port shipment from Bangkok to Rotterdam and thus violated Article 20.

1. Whether the negotiating bank is right in action?

   Yes b. No. c. Can't say

1. Is the transshipment is also to be considered in the light of Article 23 even if not mentioned in LC.

   Yes b. No. c. Can't say

o Mr. Prakash Kumar –Branch Manager LPBC bank, Camp branch, Pune, was approached by their client Mr.Suresh Chandra with a request to open an Import LC.
The LC was sanctioned by an appropriate authority and the importer Mr.Suresh Chandra required some time to comply with the sanction conditions like depositing of margin money etc.
The importer Mr. Suresh Chandra requested Mr.Prakash Kumar –Branch Manager LPBC bank, Pune Camp branch that though the bank can not open LC until sanction terms are compiled with , the bank should send a pre-advice of LC by SWIFT message as under:-
"Opened LC No.185/2008 on 24th April, 2008 for US$ 500000.00
Applicant: Sharmila Enterprises Pvt. Ltd.
Beneficiary: Clarisa INC, New York, USA
Covering: Titanium Plates

Whether the above Pre advice will act as LC and negotiation is possible a.

Yes b. No.

What should be further words in Pre advice to written as per UCP600 so that Pre advice does not become LC under UCP 600

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a. Pre advice b. Only consent of opening c. Details to follow d. No words are required.

o A sight payment L/C is issued for the amount of (not exceeding) $50,000, allowing partial shipment, the beneficiary presented his first shipping docs for the amount of $ 30,000 and was paid due to complying presentation. 2 days before expiry date, the issuing bank received a second shipping docs for an amount of $30,000 for payment (approval basis) due to overdrawing.

The applicant waived the discrepancy and instructed the issuing bank to notice the nominated bank and the beneficiary with the following i.e agreed for amendment in LC:
- Documents of the second shipment are accepted.
- L/C amount to be increased to $75,000
- Latest shipment date and expiry date are extended (where a third shipment can be made).

After this amendment, the beneficiary presented his 3rd shipping docs for an amount of $25,000, during the new L/C validity. As no discrepancies were found the nominated bank took them in compliance and sent them to the issuing bank after debiting the account of the issuing bank for payment.
The issuing bank rejected the claim saying that the LC is overdrawn. What is the amount of LC overdrawn according to issuing bank:
a. $30000 b. $25000 c. $15000 d. $10000

IV. ABC Bank opens an L/C calls for shipment of :
1. 100mt ("About") of "X" product
2. 200mt ("About") of "Y" product

Total LC value : not to exceed USD1,000,000. Partial shipments allowed.

Documents presented in one drawing for full LC value of USD1,000,000 but as separate sets of documents relating to each item, represented by invoices as follows :
1. 120mt of "X" at unit price of USD5,000 per mt = USD600,000
2. 160mt of "Y" at unit price of USD2,500 per mt = USD400,000

A. Should the issuing bank reject the claim for the documents presented:
   1. Yes 2. No.

B. Suppose the issuing bank rejected the claim by giving reason
   1. Quantity of product "X" overshipped
   2. Quantity of product "Y" undershipped
   Then, do you agree with the issuing bank for
   a. First reason is correct b. Second reason is wrong c. Both are wrong d. first is wrong , second is correct

C. According to UCPDC 600 the tolerance is allowed to the extent of +/- 5% and since the LC is not overdrawn then do you found that still issuing bank correct :
   1. Yes 2. No

Ans: I.1 a, 2 a II. 1. B 2.c III. c Iv. A. Yes B. b C. 1

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CHAPTER 4
FACILITIES AVAILABLE TO EXPORTERS AND IMPORTERS

I) To Exporters:-
* Exporters are provided timely and adequate credit to meet the exports commitments.
* Exporters are allowed pre and post-shipment credit at competitive interest rates.
* Export Credit is made available both in Indian Rupee and Foreign Currency as well. II)

To Importers:-

* Bank provides import loan at attractive rates to importers of imported inputs and capital goods.
* Import loan is allowed in Indian Rupee and in Foreign Currency.
* To enable importers avail of credit for their purchases, we also issue Documentary Credits (Letter of Credit and Standby Letter of Credit) favouring overseas supplier.
* Import LCs are issued and transmitted by fastest electronic means using 'SWIFT' systems. * "Trade Credit" is arranged for importers in line with RBI guidelines. We arrange 'Buyers' Credit' and 'Suppliers' Credit'. Issue of Letter of Credit, Letter of Comfort, Letter of Undertaking to facilitate importer arrange for 'Trade Credit' at better rates.

I) Types of Facilities for Exports
a) Rupee Export Credit (pre-shipment and post-shipment):
The bank provides both pre and post shipment credit to the Indian exporters through Rupee Denominated Loans as well as foreign currency loans in India. Credit facilities are sanctioned to exporters who satisfy credit exposure norms of the bank. Exporters having firm export orders or confirmed L/C from a bank are eligible to avail the export credit facilities.
Rupee Export Credit is available generally for a period of 180 days from the date of first disbursement. In deserving cases extension may be permitted within the guidelines of RBI. The corporate may also book forward contracts with the bank in respect of future export credit drawls, if required, as per the guidelines/directives provided by RBI.

b) Pre-shipment Credit in Foreign Currency (PCFC):
The bank offers PCFC in the foreign currency to the exporters enabling them to fund their procurement, manufacturing/processing and packing requirements. These loans are available at very competitive international interest rates covering the cost of both domestic as well as import content of the exports.
The corporate /exporters with a good track record can avail a running account facility with The bank for PCFC. PCFC is generally available for a period of 180 days from date of first disbursement. In deserving cases extension may be permitted within the guidelines of RBI.

c) Negotiation of Bills under L/C
The bank's Authorised Forex Branches are active in negotiation/discounting of sight/usance international export bills under L/Cs opened by foreign banks as well as branches of Indian banks abroad. The bank offers the most competitive rates. These transactions are undertaken by our branches within The bank/Country Exposure ceilings prescribed by The bank.

d) Export Bill Rediscounting:
The bank provides financing of export by way of discounting of export bills, as a post shipment finance to the exporters at competitive international rate of interest. This facility is available in four currencies i.e. US$, Pound Sterling, Euro and JPY.
The export bills (both Sight and Usance) drawn in compliance of FEMA can be purchased/ discounted.
Exporters can avail this facility from The bank to cover the bills drawn under L/C as well as other export bills.

e)Bank Guarantees:

The bank, on behalf of exporter constituents, issues guarantees in favour of beneficiaries abroad. The guarantees may be Performance and Financial. For Indian exporters, guarantees are issued in compliance to RBI guidelines.

II) Types of Facilities for Importers:-

a. <u>Collection of Import Bills</u>:The bank has correspondent relationship with reputed International banks throughout the world and can thus provide valuable services to importers who may be importing from any part of the Globe. The import bills are collected by our Authorised Forex Branches at very competitive rates. The import bills drawn on customers of other branches are also collected through these branches.

b) <u>Letter of Credit:</u>

On account of the bank's presence in international market for decades, the bank has established itself as a well known international bank. L/Cs of the bank is well accepted in the International market. For any special requirement the bank can get the L/C confirmed by the top international banks.

Thus the bank's L/C facility for the purchase of goods/services etc. fulfills the requirements of all importers to arrange a reliable supply. The bank offers this facility to importers in India within the ambit of FEMA and Exim policy of Govt. of India. The bank uses state of the art SWIFT network to transmit L/Cs and with a worldwide network of correspondents and our overseas branches facilitates prompt & efficient services to the importers.

L/C facility is granted to the importers on satisfying credit exposure norms of the bank.

c) <u>Financing of import</u>

Usance L/C facility:- The bank's Usance L/C facility provides the importer an opportunity to avail credit from their supplier/supplier's bank.

d) <u>Deferred Payment Guarantee/Standby LC:</u>- The bank's Deferred Payment Guarantee/Standby LC facility also provides the importer an opportunity to avail credit from their supplier/supplier's bank.

e) <u>Rupee finance:-</u> The bank also offers to Indian importers Rupee finance for payment of goods and services imported from abroad under its various Rupee credit facilities on satisfying credit exposure norms of The bank.

d) <u>Foreign Currency Loans:-</u>Short term External Commercial Borrowings or Trade Credits for less than three years as permitted by RBI for imports into India is allowed by our overseas branches to Indian importers at very competitive rates. These are generally backed by L/Cs opened by importer's bank. Indian importers can also avail this facility from our overseas branches as roll-over credit on their bank agreeing to extend the L/C in favour of our overseas branches.

e) <u>Bank Guarantees:</u>

The bank, on behalf of importer constituents or other customers, issues guarantees in favour of beneficiaries abroad. The guarantees may be both Performance and Financial.

5. REMITTANCES

The banks, through its worldwide network of correspondents, Indian branches and overseas branches, offers prompt inward and outward foreign remittance facilities at very competitive rates. The use of SWIFT network adds to reliability and efficient handling.

The remittances are handled by our Authorised Forex Branches. The outward remittances of customers of other branches are also remitted through these branches. Through our well-spread network of branches in India, inward remittances reach every nook & corner in India. The bank has tie-up arrangements with Western Union Money Transfer.

<u>Important RBI Guidelines on Rupee/Foreign Export Credit: Preshipment Rupee Export Credit:-</u>

01. Rupee Pre-shipment Credit/Packing Credit

- 'Pre-shipment/Packing Credit is the working capital finance granted to an exporter for purchase, processing, manufacturing or packing of goods prior to shipment/working capital expenses towards rendering of services against LCs or confirmed/irrevocable order or any other evidence of an order for export.
- The period of advance is to be decided by the Banks based on relevant factors. However, if the

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finance is not adjusted by submission of export documents within 360 days from the date of advance, it ceases to qualify for concessional rate of interest ab initio. Refinance from RBI is available for a period of 180 days.

• The facility may be released in one lump sum or in stages as per the requirement for executing the orders / LC. Stage wise release accounts may be maintained depending upon the types of goods/services to be exported. Banks should also keep a close watch on the end-use of the funds, besides monitoring the progress of execution of the orders.

• Liquidation of the export credit facility may be out of the proceeds of the bills drawn thereby converting the pre-shipment into post-shipment credit. It can also be liquidated out of the balances in the Exchange Earners Foreign Currency A/c (EEFC A/c) as also from rupee resources of the exporter to the extent exports have actually taken place. If not so liquidated/ repaid, banks are free to decide the rate of interest from the date of advance.

• The exporter is permitted to liquidate the packing credit in excess of the exports due to wastage, etc. by export bills drawn in respect of by-product like cashew shell oil, etc.

• For the packing credit covering non-exportable portion in respect of export of agro-based products like tobacco, pepper, cardamom, cashew nuts etc., banks are required to charge commercial rate of interest applicable to the domestic advance from the date of advance of packing credit and that portion of the packing credit would not be eligible for any refinance from RBI.

• The advance in excess of the export order in respect of HPS groundnut and de-oiled / defatted cakes is required to be adjusted either in cash or by sale of residual by-product oil within a period not exceeding 30 days from the date of advance to be eligible for concessional rate of interest.

• Banks would provide operational flexibility for repayment/liquidation of EPC with export documents relating to other export order for the same or other commodity exported or the existing packing credit may also be marked-off with proceeds of export documents against which no packing credit has been drawn by the exporter to clients who have a good track record. These relaxations should not be extended to transactions of sister / associate / group concerns.

1.1‘Running Account’ Facility

• Pre- shipment export credit facility in respect of any commodity without insisting lodgement of LC or export orders which should be produced within a reasonable period of time to be decided by the banks. This facility is being extended only to those exporters whose track record has been good as also to EOUs/ Units in Free Trade Zones / EPZs and SEZs. Running account facility should not be granted to sub suppliers.

1.2 Rupee Pre-shipment Credit to Specific Sectors/Segments

• Banks are permitted to grant Rupee Export Packing Credit to Manufacturer Suppliers for Exports Routed through STC/MMTC/Other Export Houses, Agencies etc. Such advances will be eligible for refinance subject to some conditions including obtaining a letter from the export house setting the details of the export order, etc.

1.3 Rupee Export Packing Credit to Sub-Suppliers

• Packing credit can be shared between an Export Order Holder (EOH) and sub-supplier of raw materials, components etc. of the exported goods as in the case of EOH and manufacturer suppliers, subject to the condition that it cannot be made available to Running Account facility.

• The scheme will cover the L/C or export order received in favour of Export Houses/Trading Houses/Star Trading Houses etc. or manufacturer exporters only. The scheme should be made available to the exporters with good track record. Banks may approach the ECGC for availing suitable cover in respect of such advances.

1.4 Rupee Pre-shipment Credit to Construction Contractors

• The Packing Credit facility can be granted to the construction contractors to meet their initial working capital requirements (preliminary expenses) for execution of contracts abroad on the basis of a firm contract secured from abroad, in a separate account.

• The advances should be adjusted within 365 days of the date of advance by negotiation of bills relating to the contract or by remittances received from abroad in respect of the contract executed abroad. To the extent the outstanding in the account are not adjusted in the stipulated manner,

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banks may charge normal rate of interest on such advance.

1.5 Export of Services
• Pre-shipment and post-shipment finance may be provided to exporters of all the 161 tradable services covered under the General Agreement on Trade in Services (GATS). All provisions of the circular shall apply mutatis mutandis to export of services as they apply to export of goods unless otherwise specified.
• Exporters of services qualify for working capital export credit (pre and post shipment) for consumables, wages, supplies etc.
1.6 Export Credit to Processors/Exporters-Agri-Export Zones
• Export processing units set up in Agri- Export Zones may be provided packing credit for the purpose of procuring and supplying inputs to the farmers so that quality inputs are available to them which in turn will ensure that only good quality crops are raised, besides advantages of economics of scale.
1.7 Export Credit Insurance Whole Turnover Packing Credit (ECIB-WTPC)
• Banks are eligible to obtain Whole-Turnover Packing Credit (ECIB-WTPC) for all its packing credit accounts on payment nominal guarantee fee which is to be borne by the exporters. The period of cover is for 12 months. It gives protection to the banks against losses that may be incurred in extending packing credit advances due to protracted default or insolvency of the exporter -client. The coverage is available for banks taking the cover for the first time is 75% upto Grade Percentage limit fixed and 65% beyond (For others varies from 55% to 75% depending on claim premium ratio of the bank). For small exporters/SSIU, it is 90%. Banks are required to submit Monthly declaration along with premium amount. Any extension of due date beyond 360 days should be approved by the ECGC.
02. Post shipment Rupee Export Credit
• 'Post-shipment Credit' is the working capital facility granted or any other credit provided by a bank to an exporter of goods / services from the date of extending credit after shipment of goods / rendering of services to the date of realization of export proceeds. As per the extant instructions, the period prescribed for realization of export proceeds is 12 months from the date of shipment.
• Post-shipment advance are made available in the form of - (i) Export bills purchased/discounted/negotiated. (ii) Advances against bills for collection. (iii) Advances against duty drawback receivable from Government.
• Post-shipment credit is to be liquidated by the proceeds of export bills received from abroad in respect of goods exported / services rendered. It can also be repaid / prepaid out of balances in Exchange Earners Foreign Currency Account (EEFC A/C) as also from proceeds of any other unfinanced (collection) bills.
2.1 Rupee Post shipment Export Credit:

Demand Bills	Normal Transit Period (NTP)*
Usance Bills	Max. 365 days from the date of shipment (incl. of NTP)
Overdue bill – Demand bill	Not paid within NTP plus grace period
Usance Bill	Not paid on due date

* Average period involved from date of negotiation/purchase/discount till the receipt of proceeds in the Nostro account of the Bank.

2.2 Advances against Undrawn Balances on Export Bills
• Banks are permitted to grant advances against the undrawn balances at concessional rate for a maximum period of 90 days provided such remittances are received within 180 days after expiry of NTP in case of demand bills and due date in case of usance bills. For the period beyond 90 days, the rate of interest specified for the category 'ECNOS' (Export Credit Not Otherwise Specified) at post-shipment stage may be charged.

2.3 Advances against Retention Money

• Banks may consider granting advance against retention money based on the nature of the export order like turnkey projects, etc. Such finance are subject to some guidelines as set out by RBI and listed in the M. Circular dt. 01.07.2011. No advances to be granted against retention money relating to services portion of the contract.

2.4 Export on Consignment Basis

• Export on consignment basis should be at par with exports on outright sale basis on cash terms in matters regarding the rate of interest to be charged by banks on post-shipment credit.

• For pre-shipment finance against the exports of precious and semi- precious stones on consignment exports, is adjusted as soon as export takes place, by transfer of the outstanding balance to a special (post-shipment) account which in turn, should be adjusted as soon as the relative proceeds are received from abroad but not later than 365 days from the date of export or such extended period as may be permitted by Foreign Exchange Department, RBI. Balance in the special (post-shipment) account will not be eligible for refinance from RBI.

• RBI (FED) permits on case to case basis longer period up to 12 months from the date of shipment for realization of proceeds of exports in case of Consignments Exports to CIS and East European Countries, Consignment exports to Russian Federation against repayment of State Credit in rupees, Exporters who have been certified as 'Status Holder' in terms of Foreign Trade Policy, and Cent percent EOU and units set up under Electronic Hardware Technology Park, Software Technology Park and Bio-Technology Park Schemes. In case of Exports through the Warehouse–cum-Display Centers abroad realization of export proceeds has been fixed upto 15 months from the date of shipment.

2.5 Export of goods for Exhibition and Sale

• Export of goods for exhibition and sale are eligible for export finance both pre and post shipment stages.

03. INTERST ON RUPEE EXPORT CREDIT

• With effect from 01.07.2010, interest rates applicable for all tenors of rupee export credit advances are at or above Base Rate. Prior to the period, it was not exceeding BPLR minus 2.5% per annum.

• If pre-shipment advances are not liquidated from proceeds of bills on purchase, discount, etc. on submission of export documents within 360 days from the date of advance, the advances will cease to qualify for prescribed rate of interest for export credit ab initio. Such credits will be termed as 'ECNOS' and banks may charge interest rate prescribed for 'ECNOS' pre-shipment

• If exports do not materialize at all, banks should charge on relative packing credit domestic lending rate plus penal rate of interest, if any, to be decided by the banks on the basis of a transparent policy approved by their Board.

3.1 ECNOS

• Banks are free to decide the rate of interest keeping in view of BPLR and spread guidelines in respect of Export Credit Not Otherwise Specified (ECNOS). No penal interest to be charged on
ECNOS.

Period within which export value of goods/software to be realised :- Foreign Exchange Management (Export of Goods & Services) (Amendment) Regulations, 2014:

The amount representing the full export value of goods or software exported shall be realised and repatriated to India within Nine months from the date of export.

Provided that where the goods are exported to a warehouse established outside India with the permission of the RBI, it will be as soon as it is realised and in any case within fifteen months from the date of shipment of goods; Provided further that the RBI, or subject to the directions issued by that Bank in this behalf, the authorised dealer may, for a sufficient and reasonable cause shown, extend the said period of Nine months or fifteen months, as the case may be.

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CHATPER 5
Risk in international trade

International trade is exchange of capital, goods, and services across international borders or territories.. In most countries, it represents a significant share of gross domestic product (GDP). While international trade has been present throughout much of history (see Silk Road, Amber Road), its economic, social, and political importance has been on the rise in recent centuries.
Industrialization, advanced transportation, globalization, multinational corporations, and outsourcing are all having a major impact on the international trade system. Increasing international trade is crucial to the continuance of globalization. Without international trade, nations would be limited to the goods and services produced within their own borders.
Companies doing business across international borders face many of the same risks as would normally be evident in strictly domestic transactions. For example,

Buyer insolvency (purchaser cannot pay);
- Non-acceptance (buyer rejects goods as different from the agreed upon specifications);
- Credit risk (allowing the buyer to take possession of goods prior to payment);
- Regulatory risk (e.g., a change in rules that prevents the transaction);
- Intervention (governmental action to prevent a transaction being completed);
- Political risk (change in leadership interfering with transactions or prices); and
- War and other uncontrollable events.

In addition, international trade also faces the risk of unfavorable exchange rate movements (and, the potential benefit of favorable movements)

ECGC
A. What is ECGC?
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credit.

managed by a Board of Directors comprising representatives of the G

India, banking, insurance and exporting community.

ECGC is the fifth largest credit insurer of the world in terms of coverage of national exports. The present paid- up capital of the company is Rs.800 crores and authorized capital Rs.1000 crores.

B. What does ECGC does?

1.Offers insurance protection to exporters against payment risks
2.Provides guidance in export-related activities
3.Makes available information on different countries with its own credit ratings
4.Makes it easy to obtain export finance from banks/financial institutions
5.Assists exporters in recovering bad debts
6.Provides information on credit-worthiness of overseas buyers

C. What is the Need for export credit insurance?

Payments for exports are open to risks even at the best of times. The risks have assumed large proportions today due to the far-reaching political and economic changes that are sweeping the world. An outbreak of war or civil war may block or delay payment for goods exported. A coup or an insurrection may also bring about the same result. Economic difficulties or balance of payment problems may lead a country to impose restrictions on either import of certain goods or on transfer of payments for goods imported. In addition, the exporters have to face commercial risks of insolvency or protracted default of buyers. The commercial risks of a foreign buyer going bankrupt or losing his capacity to pay are aggravated due to the political and economic uncertainties. Export credit insurance is designed to protect exporters from the consequences of the payment risks, both political and commercial, and to enable them to expand their overseas

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business without fear of loss.

To protect such exporters, ECGC has the following types of covers.

Supply contracts and turnkey projects: For covering supply contracts and turnkey projects, specific contract/shipments policy can be taken. This policy can be for covering only political risks or for covering comprehensive risks i.e. both commercial and political risks.

Construction contract: For covering construction contract, a Construction Works policy can be obtained. This policy can be for either political risk alone or for comprehensive risk. The Comprehensive Risks Policy provides protection against commercial risks such as insolvency of buyer, protracted default, non-acceptance of goods shipped in addition to covering political risk of war, civil war, exchange transfer delay etc. The political risk policy, on the other hand, provides protection against the Political Risks Policy. Under the various export credit insurance policies, ECGC generally covers loss up to 90 per cent.

Services Contract: For covering services contract, which involves only technical and/or professional services, a Services Policy can be obtained. This also can be either for political or comprehensive risks.

Overseas Investment Insurance:-OII provides cover for the investments made by Indian corporates abroad in a joint venture or their wholly owned subsidiary (WOS) either in the form of equity or loan. The Government of India or RBI should approve the JV. The basic principle is that the investment should emanate from India and benefit of dividend/interest therefrom should accrue to India. The investment should not in any way conflict with the policy of both our government and the overseas government. Normally, there should be a bilateral agreement between India and the host country for promotion and protection of Indian investment. In case there is no such agreement the Corporation should be satisfied that the existing laws of the host country adequately safeguard Indian investment.

In addition to the policy covers, which are issued to exporters, ECGC also extends its guarantee support to banks in India against both funded and non-funded facilities extended to project exporters. The types of guarantees issued by Indian banks are:

Funded:
* Packing Credit
* Post Shipment
* Overdraft
* Rupee Loan

Non-Funded
* Bid Bond
* Advance payment
* Performance guarantee
* Retention Money guarantee
* Overseas Lending Finance guarantee

Export Credit Insurance Covers to Banks from ECGC

- Covers for working capital granted by commercial banks to Exporters at Pre shipment and Post shipment stages
- Covers available on exporter wise, bank branch wise and bank wise
- Losses due to protracted default / Insolvency of exporters covered
- Cover varies from 60% to 95% depending on the type of cover
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CHAPTER 6
Role of RBI & Exchange Control

Custodian of Foreign Exchange Reserves:
It is the responsibility of the Reserve bank to stabilize the external value of the national currency. The Reserve Bank keeps golds and foreign currencies as reserves against note issue and also meets adverse balance of payments with other counties. It also manages foreign currency in accordance with the controls imposed by the government.
As far as the external sector is concerned, the task of the RBI has the following dimensions:

- To administer the foreign Exchange Control;
- To choose, the exchange rate system and fix or manages the exchange rate between the rupee and other currencies;
- To manage exchange reserves;
- To interact or negotiate with the monetary authorities of the Sterling Area, Asian Clearing Union, and other countries, and with International financial institutions such as the IMF, World Bank, and Asian Development Bank.

The RBI is the custodian of the country's foreign exchange reserves, id it is vested with the responsibility of managing the investment and utilization of the reserves in the most advantageous manner. The RBI achieves this through buying and selling of foreign exchange market, from and to schedule banks, which, are the authorized dealers in the Indian, foreign exchange market. The Bank manages the investment of reserves in gold counts abroad' and the shares and securities issued by foreign governments and international banks or financial institutions.
Before going ahead with FEDAI Rules, let us see about Nostro, Vostro & Loro accounts maintained by Authorised dealers:

The Foreign Exchange (FX) Market is one of the biggest and most liquid markets in which currencies are traded over the counter (OTC) involving players like central banks, corporate majors, hedge funds, investment banks, commercial banks etc. It aids activities such as cross-border trade, mergers & acquisitions, tourism etc. In order to deal in the Foreign Exchange Market and transact in foreign currencies, banks maintain accounts with other banks globally. This is known as a Nostro Account. For instance, consider two banks: ABC Bank, New York and XYZ Bank, Mumbai. For XYZ Bank, its account in ABC Bank is a 'Nostro Account' (My account with you) and ABC Bank's account with it is a 'Vostro Account' (your account with me). 'Nostro' and 'Vostro' are Italian words for "Our" and "Your" respectively. Reconciliation of these accounts is called Nostro Account Reconciliation or simply Nostro Reconciliation. In India only Scheduled Commercial Banks (SCB) can maintain a Nostro Account, and three types of branches are permitted to deal in them. The A category branch owns, maintains and funds this account. After the Nostro Reconciliation, they submit the statutory returns to the appropriate authorities. The B category branch can operate the account maintained by A category branches and the C category branches are the remaining Scheduled Commercial Bank branches dealing through B or A category branches for their forex transactions.
Nostro debits may arise due to:
• Honoring the payment messages sent by the bank/payment of draft issued by the bank
• Charges debited in the Nostro accounts
• Reimbursement to negotiating bank, under Letters of Credit transactions
• Payments on account of interbank deals

Nostro credit may arise due to:
• Inward remittances received on behalf of customers
• Interest amount credited
• Receipts from interbank deals
• Realization of bills sent for collection
• Reimbursement of negotiated bills

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Points to be remember:
a. The purchase/sale of currency may be spot or forward
b. Indian bank do not remit foreign currency in Nostro account from India. All receipt in FX and all payment/remittances in FX will be made through Nostro account maintained with foreign bank.
c. Forward Purchase/Sale of FX do not affect Nostro A/C because there is no delivery of currency as on date of entering such contract.
d. Spot purchase/Sales of CHF affects both exchange position as well as Nostro A/C (Cash Position)

Loro account is an account wherein a bank remits funds in foreign currency to another bank for credit to an account of a third bank. e.g . Canara Bank wants to utilize a NOSTRO account of, Say PNB, at NY, with Bank of America. This arrangement is called as LORO account.

Example for Nostro transactions:
Example No. 1 - A bank in India want to send a payment in GBP let's say the bank name is ABC Bank. This bank has a Nostro Acoount (in GBP) with a bank in UK e.g. XYZ Bank. However the beneficiary has an account with some other bank e.g. QWE Bank. This is possible with the use of Nostro account and swift messages. In the first swift message, ABC Bank will be the sender, XYZ bank will be the receiver and QWE bank will be in loop (Account with institution). In the second message XYZ bank will be the sender QWE bank will be the receiver and ABC bank will be in loop (Ordering institution) .
Example No. 2 - Cover method can be used when a bank (e.g. ABC Bank) has RMA (Relationship Management Application) with another bank (e.g. XYZ Bank) but do no maintain a Nostro Account. Here ABC can send message to XYZ Bank informing (Sender's Correspondent) that the funds will come from another bank (e.g. QWE Bank) . This Sender's Correspondent could be a common correspondent of both the banks. ABC Bank will have to send one more message. ABC Bank will have to send this message to QWE Bank.

Let me share an example to make it clear: For instance you have an account with ICICI Bank India Mumbai branch, you visit the branch and ask 1000 USD to be remitted to a person name Mr. X in New York who has an account with JP Morgan Chase. The transfer will also involve bank charges. You need to tell your bank whether the charges will be borne by you or by the beneficiary or it will be shared (i.e. shared by you and the beneficiary)
Let's say ICICI Bank has a correspondent banking relationship with JP Morgan Chase in US. ICICI Bank will debit your account to the equivalent amount in USD and will send an MT 103 message (Single Customer Credit Transfer) to JP Morgan Chase in US New York. JP Morgan will debit ICICI Bank Nostro Account (USD A/c) and will credit the beneficiary account.

Illustration 1: You as a dealer had the following position in EURO

Opening balance with Dresner, Frankfurt	20,000
	15,000
Purchased a TT	1,50,000
Issued a draft	20,000
TT remittance outward	1,25,000
Purchase and export bill payable at Milan	2,75,000
Forward sales	2,75,000
Export bill realized	45,000

What is the balance in Nostro account taking into the above transaction for the month of March'2013?

Solution: To calculate the balance one must draw up a ledger for Nostro account transactions:

Particulars	Dr.	Cr.
Opening Balance		20000
TT purchased		150000
TT Remittance	125000	
		45000
Total	125000	215000
Balance in €	90000	

Illustration 2:
You have received a SWIFT advice from Doha Correspondent stating that:
a. A sum of USD 275,000 has been credited to your New York correspondent.
b. To credit Rupee equivalent to their Rupee account with you. Interbank rates in Mumbai are $ = Rs.54.0650/0750. What rate would you apply and what Rupee equivalent would you credit to the account of DOHA correspondent with you?

Solution:- Rupee equivalent to their rupee account with you means Vostro account..
It is a sale of Rupees to DOHA Correspondent by crediting the rupees to their VOSTRO Account in India. Since this is an Inter Bank transaction no margin is to be recovered and it is assumed that the rates quotes include profit margin also.
The applicable rate for sale of rupees for buying dollars is USD = Rs.54.0650. The rupee equivalent to be credited will be Rs. 1,48,66,500.00

Illustration 3:
Your bank's rate quotation for USD on 1.5.2013 is as under :
TT (Buying) 54.35
BB (Buying) 54.35
TT (Selling) 54.80
BB (Selling) 54.90

Certain transactions has been taken place for your customers. Pick up an appropriate rate for following USD transactions to effected for giving an effect in vostro account.
a. Export bill to be purchased by you.
b. Payment of DD issued by your New York branch.
c. Retirement of Foreign Inward Bill for collection (Documentary).
d. Realization of Foreign outward Bill for Collection.
e. Remittance to US representing gift amount permissible under FEMA (1999) on behalf of your customer.

Solution:
The appropriate rate for following transactions will be :
a. Export bill to be purchased by you. = 54.35
b. Payment of DD issued by your New York branch, where you maintain your Nostro a/c. = 54.50 c. Retirement of Foreign Inward Bill for collection (Documentary). = 54.90
d. Realization of Foreign outward Bill for Collection, proceeds already credited to your Nostro a/c. = 54.50
e. Remittance to US representing gift amount permissible under FEMA (1999) on behalf of your customer. = 54.80

Mirror Account for Nostro:
Reconciliation of NOSTRO account becomes necessary because of the fact that our office of a bank maintains NOSTRO account and its replica account (mirror account) is operated by authorized branches of the said bank which results in difference of balance in the overseas bank account and the mirror account. Authorized Dealers should utilized its credit balances in NOSTRO account judiciously and ensure not to result in overdraft.
The format for such reconciliation will be like this:

XYZ Bank, Mumbai prepares a Nostro Reconciliation Statement for its USD Nostro Account with ABC Bank in its books as under.

Reconciliation Statement of ABC Nostro in USD Currency for the month ending XXX

Amounts in USD

Balance as per the Mirror Account (Debit Balance)		XXXX
Less: Un-reconciled Mirror Debits	XXXA	
Less: Un-reconciled Nostro Debits	XXXB	
Add: Un-reconciled Mirror Credits	YYYA	
Add: Un-reconciled Nostro Credits	YYYB	
Balance as per the Nostro Statement (Credit Balance)		ZZZZ

FEDAI Rules

Role of FEDAI

Established in 1958, FEDAI (Foreign Exchange Dealers' Association of India) is a group of banks that deals in foreign exchange in India as a self regulatory body under the Section 25 of the Indian Company Act (1956).

The role and responsibilities of FEDAI are as follows:

- Formulations of FEDAI guidelines and FEDAI rules for Forex business.
- Training of bank personnel in the areas of Foreign Exchange Business.
- Accreditation of Forex Brokers.
- Advising/Assisting member banks in settling issues/matters in their dealings.
- Represent member banks on Government/Reserve Bank of India and other bodies.
- Rules of FEDAI also include announcement of daily and periodical rates to its member banks.

FEDAI guidelines play an important role in the functioning of the markets and work in close coordination with Reserve Bank of India (RBI), other organizations like Fixed Income Money Market and Derivatives Association (FIMMDA), the Forex Association of India and various other market participants.

- FEDAI Rules-1-Hours-Of-Business
- FEDAI Rules-2-Export-Transactions
- FEDAI Rules-3-Import-Transactions
- FEDAI Rules-4-Merchanting-Tradeing
- FEDAI Rules-5-Clean-Instruments
- FEDAI Rules-6-Guarantees
- FEDAI Rules-7-Exchange-Contracts
- FEDAI Rules-8-Early Delivery Extension-And-Cancellation-Of-Forward -Contracts
- FEDAI Rules-9-Schedule-Of-Charges
- FEDAI Rules-10-Business-Through-Exchange-Brokers
- FEDAI Rules-11-Inter-Bank-TT-Settlement-And-Dispatch
- FEDAI Rules-12-Inter-Bank-TT-Settlement-Of-Inter-Bank-TTs-And-Despatch Fedai
- FEDAI Rules-13-Abolition-Of-Sterling-Rates-Schedule
- FEDAI Rules-14-Clarification-Explanatory-Notes-Certain-Other-Important-Information

FEDAI Rules - General Guidelines/Instructions

1. The directives issued by the Reserve Bank of India in respect of Interest rates on Export & Import Finance shall be adhered to by the Authorised Dealers.
2. The member banks are totally free to determine their own charges for various types of forex transactions, keeping in view the advice of RBI that such charges are not out of line with the average cost of providing services.
3. Authorised Dealers shall ordinarily not be parties to any guarantees for an unlimited amount and/or an unlimited period. Authorised Dealers shall ensure to include a specific clause in all the guarantees stating the exact period within which claims must be made under the guarantee besides the expiry date for the guarantee.

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o With a view to simplifying and liberalising import, authorised dealers are permitted to open standby letters of credit on behalf of their importer constituents for importing goods into India permissible under Foreign Trade Policy. RBI vide its AP (Dir Series) Circular No. 84 dated 3rd March 2003 advised the authorised dealers to open standby letters of credit subject to adherence to the guidelines issued by FEDAI. The detailed guidelines were issued by FEDAI vide Special Circular No. SPL-16/Standby LC/2003 dated 1st April 2003.

p Guidelines for calculation of Merchant Rate have been deleted from the Rule Book as the procedure for calculating the rate for Merchant transactions have been left for our member banks to decide.

	Hours of business	Each Authorised Dealer will establish its business hours for various types of foreign exchange transactions at each centre where its branches
		Authorised dealers are permitted to undertake forex business on behalf of the bank during extended hours subject to the condition that the Management in each bank lays down the working hours of the dealers.
		RBI Foreign Department have advised that exchange trading hours for inter-bank market would be from 9AM to 4PM.
	Export Transactions	Authorised Dealers will purchase only Approved Bills and the decision as to what is an approved bill lies solely with Authorised Dealers. This includes bills tendered under forward contracts, letters of credit, letters of guarantee, letters of authority, orders to negotiate, orders for payment and any other type of document of similar nature.
		Application of rate = Authorised Dealers' current bill buying rate or at the contracted rate. Interest for the normal transit period, and usance period shall be recovered simultaneously.
		Crystallisation and Recovery :-Exporters are liable for the repatriation of proceeds of the export bills negotiated/purchased/discounted or sent for collection by the AD's within time allowed for it. Considering risk in it AD's should transfer the exchange risk to the exporter by crystallising the foreign currency liability into rupee liability.
		AD's to decide on the period for crystallisation which may be linked to risk factors like credit perception of different types of exporter clients, operational aspects etc.
		Rate applicable for crystallisation: AD's TT selling rate on the date of crystallisation. Exchange difference arising out of crystallisation to be recovered from or passed on to the customer, as the case may be. Interest shall be recovered on the date of crystallisation for the period from the date of expiry of the normal transit period/notional due date to the date of crystallisation at the appropriate rate of interest as per the guidelines issued by RBI from time to time.
		Realisation of Bills after crystallization :- AD's will adjust the Rupee liability on the bill crystallised as above by applying the TT buying rate of exchange or the contracted rate. Any difference shall be recovered from/paid to the customer. Interest - From the date of crystallisation to the date of realisation of the bill shall be recovered from the customer at the appropriate rate of interest for overdue export bills as permitted by

Dishonour of Bills:-

		c. Interest at appropriate rate as per the guidelines issued by RBI.
	Interest Normal Transit Period	At the applicable rate taking into consideration of Normal Transit period. Normal transit period comprises the average period normally involved from the date of negotiation/purchase/discount till the receipt of bill proceeds in the Nostro account of the bank. Normal Transit Period is not to be confused with the time taken for the arrival of the goods at the destination.
		Normal Transit Period for purposes of all bills in Foreign Currencies 25 days
		Exports to Iraq :- 120 days from the date of shipment under UN certificate
		Normal Transit Period for purposes of bills drawn in Rupees: In the case of bills drawn under letters of credit where reimbursement is provided at the centre of negotiation: 3 days or else it will be 7 days.
		In case of export usance bills (foreign currency and rupee bills): Since due dates are reckoned from date of shipment or date of bill of exchange etc. no Normal Transit Period shall be applicable, since the actual due date is known.
		TT Reimbursement under letter of credit : Reimbursement by cable/SWIFT/Telex or other electronic means - 5 days
	Overdue Interest	To be recovered from the customer in case payment is not received on or before the expiry date of Normal Transit Period in case of demand bills, and on or before the notional due date/actual due date as the case may be in case of usance bills as per RBI directives.
	In Early realisation	Proportionate interest shall be refunded from the date of realisation i.e., by credit to nostro account in case of a foreign currency bill, and by debit to vostro account in case of a Rupee bill, upto the last date of normal transit period in the case of demand bill and upto the notional due date in case of usance bill.
	Export bills sent for collection	Application of rates :- TT buying rate ruling on the date of payment of proceeds or the forward contract rate as the case may be.
	Import Transactions	"Bills" shall include all documentary/clean bills received under letter/s of credit, standby letter's of credit, letter/s of guarantee, letter's of authority, order's to negotiate, order/s for payment and other document's or undertaking's of a similar nature or on collection basis covering imports into India.
		Application of rates for retirement of import bills : Bills selling rate ruling on the date of retirement or the forward sale contract rate as the case may be.
		Application of interest :- Bills negotiated under import letters of credit shall carry commercial rate of interest as applicable to banks' domestic advances.To be recovered from the date of debit to the AD's Nostro account to the date of crystallisation/retirement whichever is earlier.

		Crystallisation of Import Bills under Letters of Credit: All foreign currency import bills drawn under letters of credit, in the event of non-retirement shall be crystallised into Rupee liability on the 10th day after the date of receipt of documents at the letter of credit opening branch of the bank, in case of demand bills and on due date in case of usance bills at Bills Selling Rate/contracted rate as the case may be. In case the 10th day or the due date falls on a holiday or Saturday, the importer's liability shall be
		Import bill under the Forward Exchange Contract results in early/late delivery, the bank shall recover swap cost and interest, if any.
	Clean Instruments	Encashment of Inward foreign currency travellers cheques and currency notes will be at AD's option at the rates ruling on the date of such encashment. Outward remittances shall be effected at the TT selling rate of the bank ruling on the date of such remittance or at the forward contract rate.
		All foreign currency inward remittances up to an equivalent of USD 5000 shall be immediately converted into Indian Rupees.
		Beneficiary has the option of presenting the relative instrument for payment within the maximum period prescribed under FEMA, 1999 for remittances in excess of equivalent of USD 5000.
		Saturday may continue to be treated as working day except for transactions involving conversion at confirmed exchange rate (other than travel related transactions like issue/encashment of foreign currency travellers' cheques, foreign currency notes etc.).
	Foreign Exchange Contracts	Exchange contracts shall be for definite amounts and periods.
		Unless date of delivery is fixed, option period of not more than one month be specified at the discretion of the customer. If the fixed date of delivery or the last date of delivery option is a holiday/declared a holiday the delivery shall be effected/delivery option exercised on the preceding working day.
		"Ready" or "Cash" merchant contract shall be deliverable on the same day.
		A spot contract shall be deliverable on second succeeding business day.
		Merchant quotations:- The exchange rate shall be quoted in direct terms i.e., so many Rupees and Paise for 1 unit of foreign currency or 100 units of foreign currencies.
	Early Delivery, Extension and Cancellation of Foreign Exchange Contracts	Allowed at the request of the customer. It is optional for a bank unless stated to the contrary in the provisions of FEMA, 1999, a. Accept or give early delivery. b. Extend the contract.

		Early delivery:- If a bank accepts or gives early delivery, the bank shall recover/pay swap difference, if any.In all cases of early delivery of purchase or sale contracts, swap cost shall be recovered from customers irrespective of whether an actual swap is made or not. In case of outlay of fund (loss to bank) due to extension/cancellation, Interest at not below the prime lending rate of the respective AD will be charged to customer in addition to the swap cost .
		Extension: If extension is sought by the customers the contract shall be cancelled (at appropriate Selling or Buying Rate as on the date of cancellation) and rebooked simultaneously only at current rate of exchange. The difference between the contracted rate and the rate at which the contract is cancelled shall be recovered from/paid to the customer at the time of extension. Such request for extension shall be made on or before the maturity date of the contract.
		Cancellation:- Here, the AD shall recover/pay, as the case may be, the difference between the contracted rate and the rate at which the cancellation is effected.
		Rate at for cancellation: a. Purchase contracts - b. Sale contracts- Spot T.T. buying rate c.Where the contract is cancelled before maturity -appropriate forward T.T. rate
		In the absence of any instructions from the customer contracts which have matured shall be automatically cancelled on the 15th day after maturity date. In case 15th day falls on a Saturday or holiday, the contract shall be cancelled on the next succeeding working day. Here no gain will be transferred to the customer but swap cost can be recovered.
		Please refer to the illustration on the above points given after these rules..
Rule 10	Business through Exchange Brokers	Authorised Dealers make contracts through brokers such contracts shall only be made through accredited exchange brokers.No brokerage or other form of remuneration shall be paid by the Authorised Dealers to other bank employees on contracts made in respect of any foreign exchange business.
		Any accredited broker who knowingly concludes any exchange business contrary to the rules of this Association may have his recognition withdrawn and no Authorised Dealer shall transact business with him thereafter.
11	Interbank TT-Settlement and Despatch	It is absolutely necessary for AD's to reconcile all dealing items within a period of 24/48 hours by demanding cable/telex/SWIFT confirmation regarding receipt of expected credits in "Nostro" accounts from the correspondents maintaining those accounts within a maximum period of 15 days.
		Notices of non-receipt of funds in the Nostro account must be followed up by cable, telex, SWIFT etc. with defaulting counterparty banks who should immediately take up the matter with their correspondents.
		In case the seller-bank is unable to substantiate to the buyer-bank that it had intended to effect proper delivery on the settlement day, thereby amounting to 'deliberate' non-delivery of funds, the seller-bank shall pay to the buyer-bank a penalty as decided by the Managing Committee of the FEDAI or any other Sub-Committee specially appointed for the purpose by the Managing Committee. The penalty as stated above shall be in addition to the interest claim of the buyer-bank.

		Timings:- Written instructions of buyer-banks to seller- banks regarding their take -up of interbank TT transactions, not later than one hour before the close of the general banking hours of the latter.
		Settlement of interest claims on the delayed delivery of Foreign Currency Funds: In the event of late delivery of foreign currency amount of an interbank TT at the stated overseas centre, if it is London, interest for the overdue period is to be paid by the seller-bank in India at 2% over the "Barclays Bank's Base Rate" ruling on the day the remittance should have been received in London in the buyer-bank's nostro account. Further, the buyer-bank has to lodge the interest claim within 30 days from the day on which the amount should have been received. In case the buyer-bank lodges the claim after expiry of the said period of 30 days, interest at the applicable rate shall be paid for a maximum period of 60 days only or for the actual overdue period whichever is less.
		In the event of late delivery at centres other than London, interest for the number of days of the delay shall be paid in India at two per cent over the prime rate of the banks specified below at the respective centres, ruling on the day the delivery should have been made provided the buyer-bank lodges the claim for interest within 30 days from the day the delivery should have been received abroad : U.S.A. Citibank N.A. Canada Bank of Nova Scotia Japan Bank of Tokyo-Mitsubishi Ltd. Switzerland Swiss Bank Corporation EURO ABN Amro Bank In case the buyer-bank lodges the claim for interest after expiry of the aforesaid period of 30 days, interest at the applicable rate shall be paid for a maximum period of 60 days only or the actual period, whichever is less. No interest claims shall be entertained if claims are preferred after 90 days
		from the date on which the foreign currency funds should have been received by the buyer bank. Non-delivery of Foreign Currency Funds: The seller bank shall deliver
		foreign currency funds within 48 hours of the receipt of the notification from the buyer-bank. Such notification shall be sent by the buyer-bank not later than 15 days from the contracted date of delivery. Delay in payment of Rupee equivalent of interbank TTs in foreign
		currencies :The buyer bank shall pay interest for each day of delay at 2% over the NSE-MIBOR rate ruling on each such day of delay. In case the seller-bank fails to lodge the claim within the said period of 15 days, the seller-bank shall be entitled to receive interest for the maximum period of 30 days only. No interest claims shall be entertained if claims are preferred after 90 days from the date on which the rupee funds should have been received by the seller bank. Period for settlement of interest claims in Rupees:- When a bank is served
		with the notice of interest claim, it must settle the claim within 21 days of receipt thereof by making proper enquiry into its books and investigating its records. Payment of interest claim cannot be withheld for more than 21 days on the
		plea that enquiries are being made in the matter of the interest claim.

Rule 2 : Some illustration for explanation:

Illustration:- A Ltd has exported certain material to US for $ 2,00,000 on 05.01.2012 and got it discounted with X bank on 10.01.2012. The bill is usance bill for 60 days from the date of presentation of bill. The rate as quoted in spot at the time of discounting is Rs.55.128/.340. The X bank charges Rs.1000 per bill as presentation and also charges 0.150% as margin. On the basis of the above information answer the following questions:
1. What is the due date for the bill
a. 04th March,2012 b. 5th March ,2012 c. 29thMarch,2012 d. 3rd April, 2012

6. What is the amount that is will be paid to customer, if RBI states the interest rate of 9%.
a.Rs.1,07,78,915 b.Rs.1,07,77,915 c.1,08,10,223 d.1,10,51,398
Ans:- b. $ = Rs.55.128 – 0.150% margin = Rs. 55.045 * $2,00,000 = 1,10,09,000 – Rs.1000 = 1,10,08,000 – 9% Intt for 85 days (60 days + 25 days normal transit period) Rs.2,30,085 = Rs.1,07,77,915

7. If this bill got dishonoured then what will be the amount of crystallization of this bill, if the rate is $ 12.320/.440
a. 1,10,64,000 b. 1,10,88,000 c.1,11,04,600 d.1,10,47,400 Ans: c :

Refer Rule 2. And also consider the margin charged by bank.

SOME PROBLEMS ON FORWARD CONTRACT :-
The following situations are considered for explanation of Rule 8.

Cancellation of Forward Contract: In the absence of any instructions from the customer, contracts which have matured are automatically cancelled on the fifteenth day from the date of maturity. In case the fifteenth day falls on a Saturday or holiday, the contract is cancelled on the next working day. Exchange loss, if any, is recovered from the customer under advice to him. The customer is not paid any gains out of such cancellations.
Cancellation of forward contracts can be studied in two parts:-I.
Cancellation at the request of customers
II. Automatic cancellation by bank on the fifteenth day from date of maturity.

I. Cancellation at the request of customers
Situation :- Cancellation before the date of maturity: - The bank enters into an opposite contract with the customer, the new contract will have same maturity date as of old contract. That means bank will cancelled the old contract and will enter in new with same maturity date.

For example, on 10 April, 2012, a bank entered into a forward purchase contract for 1,00,000 $ @ Rs.40 maturing on 10Th June 2012. On 10 th May, 200 the customer requests the bank to cancel the contract. Suppose, on 10th May 2012, the following rates are there :
Spot : 1$ = Rs.40.00/40.10
1 month forward : 1$ =Rs.40.50/40.60
For this purpose, the bank will enter into a new forward sale contract, @ Rs.40.60, with the customer maturing 10th June, 2012. The bank recovers the difference.

Illustration:- ABC Ltd., with whom the Bank had entered into 2 months' forward purchase contract for € 5,000 @ Rs.69.50 comes to bank after 1 months and requests for cancellation of the contract. On this date, the prevailing rates are:
Spot € = Rs. 69.60 /.70
One month forward € = Rs. 69.90 / 70.04

What is the loss or gain to ABC Ltd on cancellation?
Answer: - On the day the ABC Ltd comes to the bank for cancellation, the bank will enter into a forward contract (same maturity date as that of the original) under which bank will sell 5,000 € @ Rs.70.04. On maturity, bank will sell 5,000 € to ABC Ltd (@ Rs.70.04) for Rs.3,50,200 (under the new contract) and purchase 5,000 € from the ABC Ltd (@ Rs.69.50) for Rs.3,47,500 (under the original contract). Loss to the ABC Ltd Rs.2,700. (This loss will be recovered from the ABC Ltd)

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Illustration II:- As on November 15, an exporter has booked a sell contract of US$50,000 to be delivered two months forward at a rate Rs. 48.25. The delivery date is January 15. As on December 15, he wanted to cancel the contract. The Bank charges an exchange margin of 0.15% and flat cancellation charges of Rs.250. Estimate the cash flow, with the given information as at December 15:
Interbank spot as at December 15: 47.40- 47.42
1-Month Forward: 15/30
Prime Lending Rate: 11.50% p.a

Answer:- One month before the due date the customer is cancelling the forward contract. Hence, effectively the bank can cover its position by buying one month forward. Cancellation of forward sell contract can be done by one month forward TT selling rate.
December Spot US$ Purchase rate: Rs.47.40
1-Month Forward Premium: 0.15 Rs. 47.62

Exchange Margin: 0.15%

Amount to be paid to the customer: {(Rs.48.25 – Rs.47.62)*US$ 50,000 } = Rs.39,000/
This payment is due on January 15. Since the settlement is made one month before, the PLR of 11.50% would be used for discounting the January 15 so as to pay it on December 15 and the amount would be Rs.34978/-

Situation:-Forward contract Cancellation on the date of maturity: The bank does opposite action on spot basis i.e. if under original contract the bank was to sell a currency to ABC Ltd, the bank will purchase that currency from the ABC Ltd on spot basis . The bank recovers/ pays the difference.

Illustration:- Wealthy Bank has booked a forward purchase contract for USD 1,00,000 due 14th August, 2012 @ Rs. 56.25. On maturity, the customer fails to deliver the Dollars and requests for cancellation of the contract. Spot rate on 14th August, 2012:
USD = Rs. 56.652 /.732.
What amount of gain / loss will be payable to / receivable from customer?
Answer:- On 14th August, the Bank will sell $ 1,00,000 on spot (@ Rs.56.732 per $) for Rs. 56,73,200, the bank will purchase $ 1,00,000 (@ Rs. 56.25 per $) for Rs. 56,25,000 under the original (forward) contract . Loss to the customer Rs.48,200. This loss will be recovered from the customer.

Situation:- Forward contract Cancellation 'after the date of maturity' but 'before fifteenth day after the date of maturity': The bank does opposite action on spot basis . Exchange loss , if any, is recovered from the customer under advice to him. The customer is not paid any gains out of such cancellations.

Illustration:- Bank of Hydrabad has booked a forward sale contract for USD 1,00,000 @ 54.45 due 10th June, 2012. The customer did not contact the bank on due date. However, on June 16, 2012, the customer requests the bank to cancel the contract. On this date, spot rate is Rs. 54.20 /.29. What amount of gain / loss will be payable to / receivable from customer?
Answer :- On 16th June, the Bank will sell 1,00,000 $ on under the original (forward) contract (@ Rs. 54.45 per $) for Rs. 54,45,000 the bank will purchase 1,00,000 $ (@ Rs. 54.20 per $) for Rs. 54,20,000 on spot. . Gain to the customer Rs.25,000. This gain won't be given to the customer, it will be retained by the bank.

Extension of Forward contract:-
Extension is permissible, at the customer's request, only before maturity. The bank takes two steps; (i) Cancels the original contract i.e. the bank will take all the steps required for cancellation of the contract before the date of maturity. (ii) The bank will enter into a new forward contract maturing on the date requested by the customer. The FEDAI guidelines summarize this situation

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as: Cancel and Rebook. The amount of loss / gain is received from / paid to customer at the time of the customer approaches the bank for extension.

Illustration:- On 15 June, X a customer of "Y" bank booked a forward sale contact (For bank it's a FX purchase contract) for USD 2,50,000 due July 30 @ Rs. 58.35. On 30th July. the customer requests the bank to extend the forward contact for 30th August. Foreign Exchange rates on 30th July are:
Spot 58.458/.667
Forward 30th July 57.662/.717
Forward 30th August 57.442/.537
Bank PLR rate is 12.50% p.a.

What amount of loss / gain will be receivable from / payable to customer?
Answer:
On 15th June on entering into contract with customer "X", the bank enters into simutanous contract of Forward sale in the market at a higher price than the forward price of the customer. On maturity the banks will purchase it at Rs.58.35 and will sale at higher price in forward sale contract e.g say at Rs.58.40 But, On 30th July, the customer has requested to extend the contract to 30th August. So now on 30th July, the bank will have to the bank will cancel the contract with the following calculations:
$ 2,50,000 X spot TT selling 58.667= Rs. 1,46,66,750 (that is bank has to purchase from spot and have to honour the commitment of its own other Forward sale contract)
$ 2,50,000 X 58.350 = Rs.1,45,87,500 (this is the amt of bank commitment towards the customer)

And hence here the bank suffers a loss of Rs. 1,46,66,750 – 1,45,87,500 = Rs.79,250/-

Hence, this loss of Rs.79,250 is recoverable from the customer and also recover the interest at the rate of 12.50% for 30 days = Rs.79,250*12.50% =9,906/365*30 = Rs.814/-

Early Delivery :-
The steps of early delivery can be divided into 3 parts: (I)
(a) Take delivery on spot basis and (b) make provisional payment on the original forward contract rate basis. The net effect of these two steps is that there will be either debit or credit balance in the customer's account. This will be settled at the time of maturity of the original contract (i.e. at the time of final settlement) along with interest. If there is credit balance in the customer's account the bank will pay interest at the rate of fixed deposit interest rate; if there is debit balance the bank will charge the customer interest at the rate of its Prime Lending Rate (PLR).

o A fresh contract for the cancellation of the original contract: Generally bank enters into an opposite forward contract with the market after the forward contract with the customer, and hence in case of early delivery bank is required to reverse the contract as entered in original contract after the early delivery.The new contract will have same maturity date as that of old contract (which is to be cancelled).

o On maturity : The bank will execute both the forward contracts (original contract as well as the contract entered on the date of early delivery). Under the original contract the bank will purchase the foreign currency and under the new contract (entered on the date of early delivery) the bank will sell the foreign currency.

Illustration:-
Suppose, a ABC Bank has originally entered a 3 month forward purchase of $ 1,00,000 currency at a rate of Rs.54 maturing on 31st August. On 30th June customer received $ 100,000 from US company and hence he approached bank with $ 1,00,000 to exchange in Rupee (when spot rate is Rs. 54.28/.33 and forward rate is Rs.54.80/.89 for due date after 2 months) against forward contract. How much amount will be payable to customer?
Answer:-
To settle this transaction, bank will do two things:

o Bank has to Purchase $ 1,00,000 at agreed rate Rs.54.00 and has to give Rs. 54,00,000 to customer. However, here bank is earning i.e inflow of fund and hence will this gain to customer. The profit of the bank is Purchased $1,00,000 from customer at Rs.54.00 & sold in spot at Rs.54.33 = Rs.0.33 per $ = Rs.33,000.

II) Now the bank has to enter into another forward purchase contract maturing on 31st August, i.e.due date of original contract. Because bank at the time of entering contract of purchase of $ from customer ,has entered reversed contract of Forward sale maturing on 31st August.

Now this new forward purchase bank needs to entered at Rs.54.89 maturing on 31st August. Here bank will suffer a loss to the extent of Rs.54.89 – Spot sale of Rs.54.33 = Rs.0.56 * $1,00,000 = Rs.56,000/- i.e outflow of fund and hence bank will recover interest on this amount from customer at the PLR rate.

ROLL OVER FORWARD CONTRACT:

Another application of swaps is in the "roll-over forward contracts". In some countries, forward contracts do not exist beyond certain maturities. Like, in India, it is available for maximum maturities of 6 months.

Exposures with longer terms are required to be hedged by roll-over forward contracts. Under these contracts, the exchange rate protection is provided for the entire period of the contract and the customer has to bear the roll over charges (swap charges), if any, at every roll over date.

Essentially, at every rollover date, the customer does a swap, sell spot and buy forward, or vice-versa.

E.g.- A firm has contracted a foreign currency loan of $10,00,000. The principal is to be repaid in 10 six-monthly installments. Ignoring interest payments, the firm has definite outflows of $1,00,000 every six months for the next 5 years. However, the firm cannot buy dollars more than 6 months forward out rightly at any time. It will take a rollover forward contract, which will roll over/extend for
6 months on each rollover date as follows:

1. Buy $10,00,000 for 6 months forward.
2. 6 months later take delivery of $10,00,000; use $1,00,000 to repay loan, sell spot the remaining $9,00,000 and buy them 6 months forward.

Swap charges = (Spot selling rate – Forward buying rate) 9,00,000 3.

Repeat this operation every 6 months till loan is repaid fully.

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CHAPTER 7

FOREIGN EXCHANGE MANAGEMENT ACT, 1999

BASICS

The Foreign Exchange Management Act, 1999 (FEMA) deals with cross border investments, foreign exchange transactions and transactions between residents and non-residents. It has replaced the erstwhile Foreign Exchange Regulation Act, 1973 (FERA) with effect from June 1, 2000.

The operation of FEMA is akin to any other commercial law. However as compared to most other commercial laws FEMA is one of the smallest, having only 49 Sections. If guidelines, rules, etc. are followed, the person can undertake the transaction without any approvals. If proposed transactions fall outside the guidelines, one will have to take necessary approvals. The consequence of any violation is a penalty. If penalty is not paid, then there can be prosecution.

FEMA extends to the whole of India. It also applies to all branches, offices and agencies outside India, which are owned or controlled by a person resident in India.

IMPORTANT TERMS UNDER FEMA – Section 2

1. Capital Account Transaction means a transaction which: –

• Alters foreign assets and foreign liabilities (including contingent liabilities) of Indian residents.
• Alters Indian assets and Indian liabilities of Non-residents.
• Is a Specified transaction listed in section 6(3).

Essentially this is an economic definition and not an accounting or legal definition. It is intended to cover cross border investments, cross border loans and transfer of wealth across borders. RBI has been empowered to regulate capital account transactions. Unless the transaction is permitted as per regulations, Foreign Exchange (FX) cannot be drawn for the same.

Capital account transactions though freed to a great extent, continue to be regulated by RBI. Unless RBI permits by way of rules or specific approvals, transactions cannot be undertaken. But there are two very important purposes for which RBI cannot impose any restrictions viz. drawing of foreign exchange for the repayment of any loans and for replenishing depreciation of direct investments in the ordinary course of business. (Section 6)

2. Current Account Transaction means all transactions, which are not capital account transactions. Specifically it includes:–

• Business transactions between residents and non-residents.
• Short-term banking and credit facilities in the ordinary course of business.
• Payments towards interest on loans and by way of income from investments.
• Payment of expenses of parents, spouse or children living abroad or expenses on their foreign travel, medical and education.
• Scholarships/Chairs.

Primarily there are no restrictions on current account transactions. A person may sell or draw foreign exchange freely for his current account transactions, except in a few cases where limits have been prescribed (Section 5). The Central Government has the power to regulate current account transactions. Unless the transaction is restricted, FX can be drawn for the same.

See para 7 for more details on current account transactions.

3. Person includes:–

(a) an individual
(b) a Hindu Undivided Family (HUF)
(c) a company
(d) a firm
(e) an association of persons or body of individuals, whether incorporated or not
(f) every artificial judicial person not falling in any of the above sub-clauses
(g) any agency, office or branch owned or controlled by such person.

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o Resident/Non-Resident:– If an individual stays in India for more than 182 days during the course of the preceding financial year, he will be treated as a person resident in India. There are a few exceptions as under:

- If a person goes/stays outside India for (a) taking up employment, or (b) carrying on business or vocation, or (c) for any other purpose for an uncertain period; he will be treated as a person resident outside India (non-resident). (It has been clarified that students going abroad for further studies will be regarded as non-residents.)
- If a person who is residing abroad comes to/stays in India only for (a) taking up employment, or (b) carrying on business or vocation, or (c) for any other purpose for an uncertain period; he will be treated as a person resident in India.

The term financial year means a twelve-month period beginning from April 1 and ending on March
o next.

Following persons (other than individuals) will be treated as person resident in India:

- Person or body corporate which is registered or incorporated in India.
- An office, branch or agency in India, even if it is owned or controlled by a person resident outside India.
- An office, branch or agency outside India, if it is owned or controlled by a person resident in India.

The definition is however inadequate to define residential status of a firm, an HUF, a trust or any entity which does not have to be registered.
Conversely, a non-resident means a person who is not a resident in India.

IMPORTANT FEATURES

1. All dealings in foreign exchange or foreign security can be done only through an authorized person if permitted by FEMA, rules & regulations framed there under, or by general or special permission of the RBI. Further no payments can be made by a resident to a non-resident unless permitted under FEMA (section 3).

2. Holdings / surrender of foreign currency, etc. (sections 4, 8 & 9) – Persons resident in India are primarily prohibited from acquiring, holding, owning, possessing, etc. any foreign exchange, foreign security or immovable property outside India. Also they are required to repatriate and bring to India all foreign exchange that is due to or accrued to them and deposit the same in the bank account. However they are permitted to hold foreign coins without any limit, and foreign currency notes and travellers' cheques up to US $ 2,000 or equivalent foreign currency. The foreign exchange received has to be surrendered to the authorized dealer within the prescribed time limit as mentioned below:

Services rendered, settlement of lawful obligation, inheritance, settlement, gift	180 days from date of receipt.
Unutilised foreign exchange	180 days from date of acquisition.
Unspent foreign currency notes and coins taken for travel	180 days from date of return. (In the case of an individual, if he has not deposited the same in his Resident Foreign Currency (Domestic)
Unspent foreign currency travellers' cheques taken for travel	180 days from date of return. (In the case of an individual, if he has not deposited the same in his Resident Foreign Currency (Domestic) Account.)
Other cases	180 days from date of receipt.

o Residents have been allowed to maintain foreign currency accounts in India as under:

A. EEFC ACCOUNT

A person is permitted to credit the under mentioned amounts out of his foreign exchange earnings

to his EEFC Account: -

		Limit in %
1	Status Holder Exporter (as defined in the EXIM Policy in force)	100

2	Individual professionals **	100
3	100% EOU Unit in EPZ/STP/EHTP	100
4	Any other person	100

** Professionals mean Director on Board of overseas company; Scientist /Professor in Indian University/Institution; Economist; Lawyer; Doctor; Architect; Engineer; Artist; Cost/Chartered Account; Any other person rendering professional services in his individual capacity, as may be specified by the Reserve Bank from time to time. Professional earnings including director's fees, consultancy fees, lecture fees, honorarium and similar other earnings received by a professional by rendering services in his individual capacity.
However, amounts received to meet specific obligations of the account holder cannot be credited (e.g. equity investment from a non-resident investor). The balances do not earn any interest. These funds can be used for several current account purposes. For many transactions, where there are restrictions under the current account rules, funds in EEFC account can be used without restrictions.
Units in SEZ are permitted to open, hold and maintain a Foreign Currency Account with an authorized dealer in India.

B. By Other persons i.e NRI (Non resident Indian's)

Particulars	Foreign Currency (Non-Resident) Account (Banks) Scheme (FCNR(B) Account	Non-Resident (External)Rupee Account Scheme (NRE Account)	Non-Resident Ordinary Rupee Account Scheme (NRO Account
Who can open an account	NRIs (individuals / entities of Bangladesh/ Pakistan nationality/ownership require prior approval of RBI)	NRIs (individuals / entities of Bangladesh / Pakistan nationality/ownership require prior approval of RBI)	Any person resident outside India (other than a person resident in Nepal and Bhutan). (individuals / entities of Bangladesh / Pakistan nationality / ownership as well as erstwhile OCBs require prior approval of RBI)
Joint account	In the names of two or more non-resident individuals	In the names of two or more non-resident individuals	May be held jointly with residents
Nomination	Permitted	Permitted	Permitted
Currency in which account is denominated	Pound Sterling, US Dollar, Japanese Yen, Euro, Canadian Dollar and Australian Dollar	Indian Rupees	Indian Rupees
Whether Repatriable	Repatriable	Repatriable	Not repatriable except for the following in the account - 1) current income 2) up to USD 1 million per financial year (April- March), for any bonafide purpose out of the balances in the account / sale proceeds of assets in India acquired by way of inheritance / legacy

			inclusive of assets acquired out of settlement subject to certain conditions
Type of Account	Term Deposit only	Savings, Current, Recurring, Fixed Deposit	Savings, Current, Recurring, Fixed Deposit
Period for fixed deposits	For terms not less than 1 year and not more than 5 years.	At the discretion of the bank	As applicable to resident accounts
Rate of Interest	Maturity Period: 1 year to less than 3 years: LIBOR/Swap plus 200 basis points 3 - 5 years: LIBOR/ SWAP plus 300 basis points	Banks are free to determine interest rates for term deposits w.e.f 14.08.13	Banks are free to determine interest rates for term deposits w.e.f 14.08.13
Operations by Power of Attorney in favour of a resident by the non-resident account holder	Operations on the account in terms of Power of Attorney is restricted to withdrawals for permissible local payments or remittance to the account holder himself through normal banking channels.	Operations on the account in terms of Power of Attorney is restricted to withdrawals for permissible local payments or remittance to the account holder himself through normal banking channels	Operations on the account in terms of Power of Attorney is restricted to withdrawals for permissible local payments or remittance to the account holder himself through normal banking channels

a. When a person resident in India leaves India for Nepal and Bhutan for taking up employment or for carrying on business or vocation or for any other purpose indicating his intention to stay in Nepal and Bhutan for an uncertain period, his existing account will continue as a resident account. Such account should not be designated as Non-resident (Ordinary) Rupee Account (NRO).

b. ADs may open and maintain NRE / FCNR (B) Accounts of persons resident in Nepal and Bhutan who are citizens of India or of Indian origin, provided the funds for opening these accounts are remitted in free foreign exchange, Interest earned in NRE / FCNR (B) accounts can be remitted only in Indian rupees to NRIs and PIO resident in Nepal and Bhutan.

c. In terms of Regulation 4(4) of the Notification No.FEMA.5/2000-RB dated May 3, 2000, ADs may open and maintain Rupee accounts for a person resident in Nepal / Bhutan.

Remittance of current income from NRO account :

NRI may remit outside India or may credit to NRE account current income like rent, dividend, pension, interest etc. earned in India subject to payment of applicable taxes in India.

Remittance of sale proceeds of assets from NRO account :

NRI / PIO may remit an amount, non exceeding USD 1,000,000 per financial year, being sale proceeds of financial assets/ immovable property acquired by him by way of inheritance/legacy/settlement, on production of documentary evidence in support of acquisition, inheritance or legacy of assets by the remitter, and an undertaking by the remitter and certificate by a Chartered Accountant in the formats prescribed by the Central Board of Direct Taxes.

Change of Status:
When a resident proceeds to foreign country for stay for uncertain period, the existing ordinary rupee account will be converted as NRO account. Fresh NRE account should be opened with remittance from abroad. On his return back to India for stay for uncertain period / permanent settlement, all the Non Resident running accounts will be converted as resident accounts immediately and Term Deposits will be allowed to continue till maturity.

Bank account outside India of employees of foreign companies on deputation in india
Employees of foreign companies (either foreign nationals or Indian nationals) who are on deputation in India are permitted to open, hold and maintain a foreign currency account outside India and receive salary due to them as under:–
(a) The amount of salary to be credited to such account should not exceed 75% of the salary accrued or received by the employee from the foreign company.
(b) The remaining salary shall be paid in Rupees in India.
(c) The tax on the whole salary has been paid.
Note:
'Non-Resident Indian (NRI)' means a person resident outside India who is a citizen of India or is a person of Indian origin;
'Person of Indian Origin' means a citizen of any country other than Bangladesh or Pakistan or Sri Lanka, if
a) he at any time held Indian passport; or
b) he or either of his parents or any of his grand - parents was a citizen of India by virtue of the Constitution of India or the Citizenship Act, 1955 (57 of 1955); or

c) the person is a spouse of an Indian citizen or a person referred to in sub-clause (a) or (b);
Diamond Dollar Account (DDA) :
Under the scheme of Government of India, firms and companies dealing in purchase / sale of rough or cut and polished diamonds / precious metal jewellery plain, minakari and / or studded with / without diamond and / or other stones, with a track record of at least 3 years in import / export of diamonds / coloured gemstones / diamond and coloured gemstones studded jewellery / plain gold jewellery and having an average annual turnover of Rs. 5 crores or above during the preceding three licensing years (licensing year is from April to March) are permitted to transact their business through Diamond Dollar Accounts.
They may be allowed to open not more than five Diamond Dollar Accounts with their banks.

4. CONTRAVENTION, PENALTIES & APPEALS – Sections 13 To 35
1. Penalties for contraventions under FEMA are per se monetary in nature. If any person contravenes any provisions, rules, regulations, etc. the penalty imposed may be 3 times the amount involved in contravention; and if the amount of contravention is not ascertainable, penalty can be up to Rs. 200,000. If the contravention is a continuing one, a penalty up to Rs. 5,000 per day may be imposed for every day after the 1st day during which the contravention continues.
2. The adjudicating officer may also confiscate any currency, security or property in addition to imposing penalty.
3. If a person does not pay up the penalty within 90 days, he is liable for civil imprisonment.
4. There is a right to appeal given at every stage and an appeal against an order of the Adjudicating Authority can be made to the Special Director (Appeal). An appeal against the order of the Special Director (Appeals) can be made to the Appellate Tribunal. An appeal, on questions of Law, against the order of the Appellate Tribunal can be made to the High Court.
5. A person preferring an appeal to the Special Director (Appeals) or the Appellate Tribunal can take assistance of a Chartered Accountant or Legal Practitioner.

5. DIRECTORATE OF ENFORCEMENT – SECTIONS 36 TO 38
1. The officers of the Directorate have powers to investigate contraventions referred to in section 13.
2. The powers and limitations of these officers are the same as those conferred on Income-tax Authorities under the Income-Tax Act, 1961.

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6. COMPOUNDING OF CONTRAVENTIONS

Powers for compounding of offences – RBI has been given powers for compounding all cases of contraventions other than cases under section 3(a) of FEMA. Cases of contravention under section 3(a) relate to dealing in or transfer of foreign exchange and foreign security to any person other than an authorised dealer. For these, Enforcement Directorate will be responsible. Powers of compounding with RBI should give confidence to public.

Depending on the amount involved, various officers have been designated to look into applications for compounding. The compounding authority can call for any information, record or any other documents relevant to the compounding proceedings. The compounding authority is required to pass an order within 180 days from the date of application. The sum for which the contravention is compounded has to be paid within 15 days from the date of order of compounding.

7. PERMISSIBLE TRANSACTIONS BY RESIDENTS

7. 1 Current Account Transactions (See para 2.2 for meaning)

Unless the transaction falls within the below mentioned restrictions, FX can be drawn for the same without any limit.

Broad categories of current account transactions can be classified as under:

i. Transactions for which FX withdrawal is totally prohibited such as payment for lotteries, transactions with residents of Nepal and Bhutan, etc.

ii. Transactions for which FX can be withdrawn only with prior approval of Government, such as specified transactions by PSUs, lump sum knowhow payments exceeding US $ 2 million, etc. However payments from EEFC, RFC (D) and RFC Account do not require any approval.

iii. Transactions for which FX can be withdrawn only with prior approval of Government even if payment is made from EEFC Account.

iv. Transactions for which FX can be withdrawn only with prior approval of RBI such as FX for business travel exceeding US $ 25,000, etc. However, payments from EEFC, RFC (D) and RFC Account do not require any approval.

v. Transactions for which FX can be withdrawn only with prior approval of RBI even if payment is made from EEFC Account.

Residents are permitted to remit US $ 1,25,000 for any current and capital account purpose (except those transactions which are prohibited altogether – refer paragraph A below).

(See para 7.2.2 below for further details on investments abroad by Individuals)

<u>The details of restrictions on Current Account Transactions are as follows</u>: A.
Payments or withdrawal of FX for following purposes are totally prohibited:-1.
Travel to Nepal and Bhutan.
2. Transaction with a person resident in Nepal and Bhutan.
3. Remittance out of lottery winnings.
4. Remittance of income from racing/riding, etc. or any other hobby.
5. Remittance for purchase of lottery tickets, banned/ proscribed magazines, football pools, sweepstakes, etc.
6. Payment of commission on exports made towards equity investment in Joint Ventures/Wholly Owned Subsidiaries abroad of Indian companies.
7. Payment of commission on exports under Rupee State Credit Route, except commission up to 10% of invoice value of exports of tea and tobacco.
8. Payment related to "Call Back Services" of telephones.
9. Remittance of interest income on funds held in NRSR Scheme Account.
10. Remittance towards participation in lottery schemes involving money circulation or for securing prize money / awards, etc.

B. The following payments will require prior approval of RBI, except where the payment is made from the RFC or RFC(D) or EEFC Account of the remitter:–
1. Release of exchange exceeding US $ 10,000 or its equivalent in one calendar year, for one or more private visits to any country (except Nepal and Bhutan).
2. Exchange facilities exceeding US $ 100,000 for persons going abroad for employment.

3. Exchange facilities for emigration exceeding US $ 100,000 or amount prescribed by country of emigration.
4. Remittance for maintenance of close relatives abroad,
(i) exceeding the net salary (after deduction of taxes, contribution to provident fund and other deductions) of 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 or subsidiary or joint venture in India of such foreign company.
(ii) exceeding US $ 100,000 per year per recipient.
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 the length thereof) or for a specific job or assignment; the duration of which does not exceed three years, is a resident but not permanently resident.
5. Release of foreign exchange, exceeding US $ 25,000 to a person, irrespective of period of stay, for business travel, or attending a Conference or specialized training or for maintenance expenses of a patient going abroad for medical treatment or check-up abroad, or for accompanying as attendant to a patient going abroad for medical treatment/check-up.
6. Release of exchange for meeting expenses for medical treatment abroad exceeding the estimate from the doctor in India or hospital / doctor abroad. However, an amount up to US $ 100,000 or its equivalent can be released without insisting on any estimate from a hospital / doctor.
7. Release of exchange for studies abroad exceeding the estimates from the institution abroad or US $ 100,000 per academic year, whichever is higher.
8. a) Remittances exceeding US $ 1,000,000 per project, for any consultancy services procured from outside India.
b) Remittances exceeding US $ 10 million per project, consultancy services procured from outside India by Indian companies executing infrastructure projects.
9. Advance towards import of services in India exceeding US $ 100,000.

C. The following payments will require prior approval of RBI, except where the payment is made from the RFC or RFC(D) Account of the remitter:–
1. Commission to agents abroad for sale of residential flats/commercial plots in India, exceeding US $ 25,000 or 5% of the inward remittance (whichever is higher) per transaction.
2. Remittance exceeding US $ 100,000 or 5 % of the investment brought into India, whichever is higher, by an entity in India by way of reimbursement of pre-incorporation expenses in India.
3. Donations in excess of US $ 5,000 by Indian corporates.
4. Donations by Indian corporates, in exceeding 1% of the foreign exchange earnings during the previous 3 financial years or US $ 5 million, whichever is less, for
a) Creation of Chairs in reputed educational institutes.
b) Donations to funds (not being an investment fund) promoted by educational institutes.
c) Donation to technical institution or body or association in the field of activity of the donor company.
5. Payment for purchase of Trade Mark(s)/Patent(s).

7.2 Investments Abroad by Indian Residents

7.2.1 Joint ventures & wholly owned subsidiaries.

Automatic route (No permission required)	Investment made upto 400% of the Net worth as per the last balance sheet. Investment over 100% of net worth requires permission.
Who can set up JVs& WOS	Indian Companies & Registered Partnership firms only. Registered Trust/ Society operating hospitals in India, can invest in same sector abroad.
Prohibited activity for Investment in JVs & WOS	Portfolio Investment & Investment in banking & real estate
Way of Investment	Equity, loans or by way of guarantees.

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Other Investments Options:-

Who can invest & upto what amount	a. Listed Indian company upto 50% of list net worth as per last audited Balance sheets. b. Indian MF registered with SEBI upto US$ 7 billion. c. Indian VC registered with SEBI - Upto to US$ 500 million in equity/ Equity linked investment of off shore VC after SEBI approved.
Agriculture operations overseas Who can invest& upto what amount.	Indian Company & registered partnership upto 400% of its Net worth.
Investment by regional Star Exporters.	Proprietory Concern/unregistered Partnership firm, who exports for more than 15cr pa. KYC compiled & exports outstanding not exceeding 10% of average export realization of last 3 yrs, can invest max of avg. 3 yrs export realization of 200/- of their net owned Funds, whichever is lower.

7.2.2 Remittance under the Us $ 1,25,000 Scheme w.e.f June 3, 2014

An individual resident in India is permitted to remit up to US $ 1,25,000 per calendar year for any legal and lawful purpose without obtaining prior permission of RBI. The individual can use said facility for any current account transaction, acquisition of any movable and/or immovable property, remittance towards gift and donation, investment in overseas companies or opening of a bank account outside India. However, remittances cannot be made to Bhutan, Nepal, Mauritius or Pakistan or countries identified as "non co-operative countries and territories" by the Financial Action Task Force. Currently (i.e., as per list updated as on February 17, 2006), the countries where investment cannot be made are Myanmar, Nigeria. The updated list can be seen at the website of FATF - http://www.fatf-gafi.org. An application cum declaration form is required to be filed with the A. D.

7.2.3 Acquisition and Transfer of Immovable Property outside India

Immovable property outside India can be acquired by following persons:

A. INDIVIDUALS

	Indian Nationals	Indian Nationals	Foreign Nationals
	Resident in India	Resident Outside	Resident in/
o	By way of gift or inheritance from any person resident in India but who was a non-resident and had acquired the property while he was a non-resident	No restrictions	No restrictions
/	By purchase out of funds held in RFC Account		
	OTHERS		
	Indian Companies	Subsidiaries of	Companies

		Indian Companies	
1	For their business	No restrictions	No restrictions

7.2.4 Borrowings from Non-residents

Who can borrow?	
	those in the hotel, hospital, software sectors except financial intermediaries (such as banks, FIs, housing finance companies and NBFCs) are eligible to borrow. b. Financial institutions dealing exclusively with infrastructure or export
	finance such as IDFC, ILFS, Power Finance Corporation, Power Trading Corporation, IRCON and EXIM Bank will be considered on a c. Banks and financial institutions which had participated in the textile or
	steel sector restructuring package as approved by the Government d. Foreign Currency Convertible Bonds (FCCB) by housing Finance
	e. Indian Companies engaged in the development of integrated
	townships including housing, commercial premises, hotels resorts, city and regional level urban infrastructure facilities such as roads and bridges, mass rapid transit systems and manufacture of building materials, development of land and providing allied infrastructure f. SEZ developers can avail of ECB under the Approval Route for
	providing infrastructure facilities, as defined in the ECB policy, within the SEZ. g. Micro Finance Institutions (MFIs) engaged in micro finance activities,
Purpose for which they	registered under the Societies Registration Act, 1860, MFIs registered under Indian Trust Act, 1882. a) Except for the prohibited activities, ECBs can be used for any
can borrow?	bonafide business requirement such as import of capital goods, new projects, modernization / expansion of existing production units, etc. NO ECB is allowed for working capital, onward lending & for investing in real estate b. Utilization of ECB proceeds is permitted for direct investment in Joint
	Ventures (JV) / Wholly Owned Subsidiaries (WOS) either by way of fresh investment or expansion of existing JV / WOS including for mergers and acquisitions. c. Payment for obtaining licence/permit for 3G Spectrum.
	d. Indian companies in manufacturing and infrastructure sector and
From whom can be	having foreign exchange earnings, for repayment of outstanding Rupee loans towards capital expenditure and/or fresh Rupee capital expenditure under the approval route. The overall ceiling for such ECBs would be USD 10 billion. a. International banks, international capital markets, multilateral financial
borrowed?	institutions such as IFC, ADB, CDC etc. b. Export credit agencies, Suppliers of equipment, foreign collaborators
Limit upto which ECB	and foreign equity holders. A. Automatic Route
can be raised?	I. Maximum other than those in the hotel, hospital and software sectors is USD 750 million or its equivalent during a financial year. II. Corporates in the services sector viz. hotels, hospitals and software sector are allowed to avail of ECB up to USD 200 million or its equivalent in a financial year for meeting foreign currency and/ or

Rupee capital expenditure for permissible end-uses. The proceeds of the ECBs

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	should not be used for acquisition of land. III. NGOs engaged in micro finance activities and Micro Finance Institutions (MFIs) can raise ECB up to USD 10 million or its equivalent during a financial year. B. Approval Route: Limit above the automatic route will be considered on case by case basis.
Restriction on total cost of borrowing	Minimum Average Maturity Period 3 years to 5 years : 350 basis points over 6 months LIBOR More than five years: 500 basis points over 6 months LIBOR (These are All-in-cost ceilings) In the case of fixed rate loans, the swap cost plus margin should be the
	All-in-cost includes rate of interest, other fees and expenses in foreign currency except commitment fee, pre-payment fee, and fees payable in Indian Rupees. Further, total cost will also exclude payment of withholding tax in Indian Rupees.
ECB Maturity	a) ECB up to US $ 20 million or equivalent : Minimum average maturity of three years b) ECB above US $ 20 million and up to US $ 750 million or equivalent with minimum average maturity of five years c) ECB up to US $ 20 million can have call/put option provided the minimum average maturity of 3 years is complied before exercising

7.4.1 Borrowings through Loans / Deposits

Indian Companies, other Body Corporates, Indian Proprietary Concerns and Firms can accept fresh deposits from NRI only if the deposit is by way of debit to the NRO account of the lender and the amount deposited does not represent inward remittances or transfer from NRE/FCNR (B) Accounts into the NRO Account of the lender. However, they are permitted to hold and renew on maturity existing deposits received by them on repatriation as well as non-repatriation basis.

Resident Individuals are permitted to avail of interest free loans up to US $ 250,000 from their NRI / PIO relatives subject to certain conditions.

Special permission of the RBI will be required in case where deposits / loans do not fulfil the specified criteria or where the deposits/loans are on repatriation basis in the case of proprietary concerns and firms.

8. PERMISSIBLE TRANSACTIONS BY NON-RESIDENTS:

8. 1 Foreign Direct Investment (FDI) in India is : FDI(Foreign Direct Investment):

- Undertaken in accordance with the FDI Policy which is formulated and announced by the Government of India. The Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India issues a "Consolidated FDI Policy Circular " on an yearly basis on March 31 of each year (since 2010) elaborating the policy and the process in respect of FDI in India. The latest "Consolidated FDI Policy Circular" dated April 5, 2013 is available in public domain and can be downloaded from the website of Ministry of Commerce and Industry, Department of Industrial Policy and Promotion –
- http://www.dipp.nic.in/English/Policies/FDI_Circular_01_ 2013.pdf governed by the provisions of the Foreign Exchange Management Act (FEMA), 1999. FEMA Regulations which prescribe amongst other things the mode of investments i.e. issue or acquisition of shares / convertible debentures and preference shares, manner of receipt of funds, pricing guidelines and reporting of the investments to the Reserve Bank. The Reserve Bank has issued Notification No. FEMA 20 /2000 -RB dated May 3, 2000 which contains the Regulations in this regard. This Notification has been amended from time to time.

Entry routes for investments in	investments can be made in shares, mandatorily and fully convertible debentures and mandatorily and fully convertible preference shares of an

India	Indian company by non-residents through two routes: a. Automatic Route: Under the Automatic Route, the foreign investor or the Indian company does not require any approval from the Reserve Bank or Government of India for the investment. b. Government Route: Under the Government Route, the foreign investor or the Indian company should obtain prior approval of the Government of India(Foreign Investment Promotion Board (FIPB), Department of Economic Affairs (DEA), Ministry of Finance or Department of Industrial Policy & Promotion, as the case may be) for the investment.
List of activities or items in which FDI is prohibited	(i) Foreign investment in any form is prohibited in a company or a partnership firm or a proprietary concern or any entity, whether incorporated or not (such as, Trusts) which is engaged or proposes to engage in the following activities: a. Business of chit fund, or b. Nidhi company, or c. Agricultural or plantation activities, or d. Real estate business, or construction of farm houses, or (ii) It is clarified that "real estate business" means dealing in land and immovable property with a view to earning profit or earning income there from and does not include development of townships, construction of residential / commercial premises, roads or bridges, educational institutions, recreational facilities, city and regional level infrastructure, townships. It is further clarified that partnership firms /proprietorship concerns having investments as per FEMA regulations are not allowed to engage in print media sector. (iii) In addition to the above, Foreign investment in the form of FDI is also prohibited in certain sectors such as (a) Lottery Business including Government /private lottery, online lotteries, etc. (b) Gambling and Betting including casinos etc. (c) Business of Chit funds (d) Nidhi company (e) Trading in Transferable Development Rights (TDRs) (f) Real Estate Business or Construction of Farm Houses (g) Manufacturing of Cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes (h) Activities / sectors not open to private sector investment e.g. Atomic Energy and Railway Transport (other than Mass Rapid Transport Systems). Note: Foreign technology collaboration in any form including licensing for franchise, trademark, brand name, management contract is also prohibited for Lottery Business and Gambling and Betting activities.
Eligibility for Investment in India	(i) A person resident outside India or an entity incorporated outside India, can invest in India, subject to the FDI Policy of the Government of India. A person who is a citizen of Bangladesh or an entity incorporated in Bangladesh can invest in India under the FDI Scheme, with the prior approval of the FIPB. Further, a person who is a citizen of Pakistan or an entity incorporated in Pakistan, may, with the prior approval of the FIPB, can invest in an Indian company under FDI Scheme, subject to the prohibitions applicable to all foreign investors and the Indian company, receiving such foreign direct investment, should not be engaged in sectors / activities pertaining to defence, space and atomic energy. (ii) NRIs, resident in Nepal and Bhutan as well as citizens of Nepal and Bhutan are permitted to invest in shares and convertible debentures of Indian companies under FDI Scheme on repatriation basis, subject to the condition that the amount of consideration for such investment shall be paid only by way of inward remittance in free foreign exchange through normal banking channels.

Investment Limits	a) Foreign Investment Limits
	The details of the entry route applicable and the maximum permissible foreign investment / sectoral cap in an Indian Company are determined by the sector in which it is operating. The details of the entry route applicable along with the sectoral cap for foreign investment in various sectors are given in sectoral investment guidelines. b) Investments in Micro and Small Enterprise (MSE) A company which is reckoned as Micro and Small Enterprise (MSE) (earlier Small Scale Industrial Unit) in terms of the Micro, Small and Medium Enterprises Development (MSMED) Act, 2006, including an Export Oriented Unit or a Unit in Free Trade Zone or in Export Processing Zone or in a Software Technology Park or in an Electronic Hardware Technology Park, may issue shares or convertible debentures to a person resident outside India (other than a resident of Pakistan and to a resident of Bangladesh under approval route), subject to the prescribed limits as per FDI Policy, in accordance with the Entry Routes and the provision of Foreign Direct Investment Policy, as notified by the Ministry of Commerce & Industry, Government of India, from time to time. Any Industrial undertaking, with or without FDI, which is not an MSE, having an industrial license under the provisions of the Industries (Development & Regulation) Act, 1951 for manufacturing items reserved for the MSE sector may issue shares to persons resident outside India (other than a resident/entity of Pakistan and to a resident/entity of Bangladesh with prior approval FIPB), to the extent of 24 per cent of its paid-up capital or sectoral cap whichever is lower. Issue of shares in excess of 24 per cent of paid-up capital shall require prior approval of the FIPB of the Government of India and shall be in compliance with the terms and conditions of such approval.
Euro Issues, ADR/GDR Issues	No end-use restrictions except prohibition on investment in stock market & real estate – A broker can purchase shares on behalf of Non-Residents and convert the shares so purchased into ADR/GDR – Two-way fungibility allowed in case of ADR/GDR issues; i.e., ADR/GDR can be converted into underlying equity shares in India and shares already issued in India can be converted into ADR/GDR and issued abroad. – Funds raised can be brought into India or retained abroad for meeting future foreign exchange requirements.
Investment instruments	Purchase of shares and convertible debentures issued by Indian companies under the Portfolio Investment Scheme (PIS).
Who can invest	Foreign Institutional Investors (FIIs) registered with SEBI, NRIs, SEBI approved sub accounts of FIIs (sub accounts),
Limits of Investment	A. FIIs (a) An Individual FII/ SEBI approved sub accounts of FIIs can invest up to a maximum of 10 per cent of the total paid-up capital or 10 per cent of the paid-up value of each series of convertible debentures issued by the Indian company. The 10 per cent limit would include shares held by SEBI registered FII/ SEBI approved sub accounts of FII under the PIS (by way of purchases made through a registered broker on a recognized stock exchange in India or by way of offer/private placement) as well as shares acquired by SEBI registered FII under the FDI scheme. (b) Total holdings of all FIIs / SEBI approved sub accounts of FIIs put together shall not exceed 24 per cent of the paid -up capital or paid -up value of each series of convertible debentures. This limit of 24 per cent can be increased to the sectoral cap / statutory limit, as applicable to the Indian company concerned, by passing of a resolution by its Board of Directors, followed by a special resolution to that effect by its General Body which

should necessarily be intimated to the Reserve Bank of India immediately as

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	hitherto, along with certificate from the Company Secretary stating that all the relevant provisions of the extant Foreign Exchange Management Act, 1999 regulations and the Foreign Direct Investment Policy, as amended from time to to time have been complied with.
	B. NRIs (a) NRIs are allowed to invest in shares of listed Indian companies in recognised Stock Exchanges under the PIS. (b) NRIs can invest through designated ADs, on repatriation and non-repatriation basis under PIS route up to 5 per cent of the paid- up capital / paid-up value of each series of debentures of listed Indian companies. (c) The aggregate paid-up value of shares / convertible debentures purchased by all NRIs cannot exceed 10 per cent of the paid-up capital of the company / paid-up value of each series of debentures of the company. The aggregate ceiling of 10 per cent can be raised to 24 per cent by passing of a resolution by its Board of Directors followed by a special resolution to that effect by its General Body which should necessarily be intimated to the Reserve Bank of India immediately as hitherto, along with Certificate from the Company Secretary stating that all the relevant provisions of the extant Foreign Exchange Management Act, 1999 regulations and the Foreign Direct Investment Policy, as amended from time to time have been complied with.
Prohibition for investments by FIIs and NRIs	• FIIs are not permitted to invest in the capital of an Asset Reconstruction Company. • Both FIIs and NRIs are not allowed to invest in any company which is engaged or proposes to engage in the following activities: i. Business of chit fund, or ii. Nidhi company, or iii. Agricultural or plantation activities, or iv. Real estate business* or construction of farm houses, or v. Trading in Transferable Development Rights (TDRs). * Real estate business" does not include construction of housing / commercial premises, educational institutions, recreational facilities, city and regional level infrastructure, townships.
Who can invest	A Non- Resident Indian (NRI) or a Person of Indian Origin (PIO) resident outside India can invest by way of contribution to the capital of a firm or a proprietary concern in India on non-repatriation basis provided: i. Amount is invested by inward remittance or out of NRE / FCNR(B) / NRO account maintained with Authorised Dealers / Authorised banks. ii. The firm or proprietary concern is not engaged in any agricultural / plantation or real estate business (i.e. dealing in land and immovable property with a view to earning profit or earning income there from) or print media sector. iii. Amount invested shall not be eligible for repatriation outside India.
	Investments with repatriation benefits NRIs / PIO may seek prior permission of Reserve Bank for investment in sole proprietorship concerns / partnership firms with repatriation benefits. The application will be decided in consultation with the Government of India.
Investment by non-residents other than NRIs / PIO	A person resident outside India other than NRIs / PIO may make an application and seek prior approval of Reserve Bank, for making investment by way of contribution to the capital of a firm or a proprietorship concern or any association of persons in India. The application will be decided in consultation with the Government of India.
Restrictions	An NRI or PIO is not allowed to invest in a firm or proprietorship concern engaged in any agricultural/plantation activity or real estate business (i.e. dealing in land and immovable property with a view to earning profit or earning income therefrom) or engaged in Print Media.

8.3 Acquisition and transfer of Immoveable Property in India

Immovable property in India can be acquired / transferred by following persons:

Table A

	Indian Nationals Resident in India	Indian Nationals Resident Outside India	Foreign Nationals Resident in/ Outside India
1	By way of gift or inheritance from any person resident in India but who was a non-resident and had acquired the property while he was a non-resident	No restrictions	No restrictions
2	By purchase out of funds held in RFC Account		

Notes:–

1. Persons of Indian Origin do not include citizens of Pakistan, Bangladesh, Sri Lanka, Afghanistan, China, Iran, Nepal or Bhutan.
2. NRI / PIO can borrow money from banks / approved housing finance companies for acquisition / repairs / renovation / improvement of residential accommodation in India.
3. NRI / PIO can repatriate equivalent to the amount of foreign exchange remitted into India at the time of purchase.
4. Payment by NRI / PIO for purchase of immovable property cannot be by way of foreign currency notes or traveller's cheques.
5. NRI / PIO employees of Indian companies in India or their branches outside India can also take loans from their employers for purchasing housing property in India or abroad or for any other purpose other than for utilizing in the following activities: -

(a) Chit fund business; (b) Nidhi company; (c) Agricultural or plantation activity or in real estate business or construction of farm houses

(d) Trading in TDR; (e) Investment in capital market including margin trading and derivatives.

Table B

Foreign Citizens Resident in India	Foreign Citizens Resident Outside India	of Foreign Concern
case of Nationals of Pakistan, Bangladesh, Sri Lanka, China, Bhutan who will require prior permission from RBI in all cases except where the immovable lease for less than 5 years	Can acquire and transfer only after prior permission from RBI Foreign Embassy / Diplomat / Consulate General other than agricultural land / plantation property / farm house only after obtaining prior p External Affairs, Government of India and	/ for carrying on its Form IPI will have to filed such acquisition

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	the consideration for acquisition is remitted from abroad	prior RBI approval.

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Foreign Exchange is a commodity. Forex transactions (sale/purchase) are regulated in India under : FEMA 1999.Objective of FEMA: To facilitate external trade and orderly management and development of inter-bank forex markets in India. Inter-bank forex market regulated in India by : RBI. Inter-bank forex market timing: 9 am to 5 pm (Saturday-closed).Foreign Currency rates are fixed in India by: Market forces of demand and supply (Higher demand - higher rate).Foreign trade is regulated by: DGFT. In India direct rates is used W.e.f. 1.8.1993.

The world trade, export and import of commodities, cross-border movement of manpower and capital, travel and tourism and export of services, all necessitate the need for exchange of currency of one country to the currency of another country. The export of goods manufactured in India, to USA, is paid in US dollars, where the exporter needs to convert the USD proceeds of the bill into Indian rupees. Similarly, import of capital goods from Germany into India, billed in Euro, is to be paid in Euro, by converting Indian rupees into Euro. Thus conversion of currencies from the currency of invoice to the home currency of the exporters will be generally required for all cross border trades. *This is Foreign Exchange.* For the Indian exporter or the importer, the US dollars or Euro is foreign exchange, while for the American (buyer of Indian goods) or the German (seller of capital goods), Indian rupee is foreign exchange. Thus, in today's world, when nations push for greater inflow or outflow of goods, capital or services, foreign exchange has become an integral part of the world financial system. The term Foreign Exchange is more broadly used to denote foreign currency, i.e. currency of any country, as well as the exchange of currency of one country into that of another.

Foreign Exchange is a commodity. Forex transactions (sale/purchase) are regulated in India under : FEMA 1999.Objective of FEMA: To facilitate external trade and orderly management and development of inter-bank forex markets in India. Inter-bank forex market regulated in India by : RBI. Inter-bank forex market timing: 9 am to 5 pm (Saturday-closed).Foreign Currency rates are fixed in India by: Market forces of demand and supply (Higher demand - higher rate).Foreign trade is regulated by: DGFT. In India direct rates is used W.e.f. 1.8.1993,.

MEANING OF FOREIGN EXCHANGE

As per Foreign Exchange Management Act 1999, foreign exchange means: "the foreign currency and includes deposits, credits and balance payable in any foreign currency, drafts, travellers cheques, letter of credit or bills of exchange, expressed or drawn in Indian currency but payable in any foreign currency, drafts, travellers cheques, letter of credit or bills of exchange drawn by banks, institutions or persons outside India, but payable in Indian currency".

In other words, the foreign exchange stock include foreign currency assets, balances kept abroad, instruments payable in foreign currency and instruments drawn abroad but payable in Indian currency. *In exchange rate system, the foreign currencies are just likecommodities having varying prices. These currencies are sold and purchased to settle transactions between various parties in various countries.*

FEATURES OF FOREIGN EXCHANGE MARKETS

Foreign exchange markets are composed of individuals, business organisations, banks, investors, users, arbitrageurs etc. who buy or sell foreign exchange. The features of these markets are:

- These markets exist around the globe.
- There are no boundaries for the markets as the markets are communication system based.
- The markets are very dynamic and by an estimate, there is fluctuation every 4 second or even earlier.
- The markets open Monday through Friday (Saturday and Sunday being closed days).
- In India, the inter-bank markets open at 9 a.m. and close at 5 p.m:
- The markets operate round the clock in one or other part of the globe due to different time zones.
- Geographically the markets extend from Tokyo & Sydney in the East to London & New York in the West.
- When the European markets open, there is already launch time for Indian markets. When Indian markets close, the US markets are about to open. Just before close of US markets, the Tokyo or Singapore markets are about to open.
- Participants in FC markets : (a) Central Banks (b) commercial banks (c) investment banks or funds (d) foreign exchange brokers (e) companies and (f)

FACTORS DETERMINING EXCHANGE RATES These factors can be (i) Fundamental reasons (2) Technical reasons (3) Speculation.Fundamental Reasons: These affect the basic economic and monetary policies of Govt. They normally affect the long term rates and include:

- Balance of payment position of the country (surplus leads to stronger currency and deficit weakens a currency).
- Economic growth rate of the GDP of the country (high growth rate leads to imports and fall in value of the currency)
- Fiscal policy followed by the country (expansionary policy leads to high economic growth).
- Monetary policy of the country.
- Interest rate structure prevalent in the country (high domestic rates lead to appreciation in currency rate).

Technical Reasons:

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Govt. controls — Lead to unrealistic value of a currency resulting in violent rates.
Freedom on capital movement or restrictions on capital movement. (capital moves from low yielding
to higher yielding currencies and affect the currency rates.
Speculation : Expectation of devaluation of currency — speculators will short sell the currency and buy back at a low rate later on. Speculative transactions provide depth and liquidity to the market.

EXCHANGERATEMECHANISM

Exchange rate is the rate at which one currency is converted into another currency (1 USD = Rs.5o.55). The price of one currency (USD here), is quoted in terms of another (Rs.). Exchange rate is a very dynamic rate and varies from minute to minute across the world, for a no. of reasons.

Liberalisation - During 1991 there was devaluation of rupee in 2 stages and wef March 1, 1992 liberalised exchange rate managementsystem (LERMS) was introduced. Resultantly all forex transactions are put through by Authorised Dealers at market determined rates of exchange. All FEX receipts are to be retained by ADs without surrendering to RBI and all FEX receipts and payments are regulated by Exchange Control.

Direct quotation - From 1993 dollar has been the intervention currency and the method of quotation has been changed to Directmethod wef Aug 1, 1993.

Buying & Selling Rates

An authorised dealer makes purchases of foreign currency (FC) and also sells it. When a bank purchases FC it is referred to as a purchase transaction for FC concerned (inflow of FC) on which buying rate is used. Encashment of a ¯travellers' cheque by a bank, is a purchase transaction as in such transaction, the bank acquires FC and parts with the home currency.
When a bank sells FC it acquires home currency and parts with FC (outflow of FC) on which selling rate is used. Issuing of a travellers' cheque is a sale transaction.

DIFFERENT TYPES OF EXCHANGE RATES

Fixed Rates: It is official rate fixed by monetary authority of a country (RBI in India). It is fixed to one or more currencies.

Floating Rate: It is a system where the exchange rates are determined by the conditions of demand for and supply of the forex in themarket. The rates fluctuate freely in the line with the demand and supply without any restrictions on buying and selling. Under this rate no par value is declared.

Flexible Rate: In this system the exchange rate is fixed but it is frequently adjusted in line with the market conditions. **Inter-Bank Rates :** In the inter-bank market, the rates are quoted both for the buying and selling the currency*like*(43.20/40), thatindicates that for one $, the market buying rate is F.s.43.20 and the selling rate Rs.43.4o. The quoting bank indicates that it is ready to buy dollar at Rs.43.20 and sell at

The thumb rule for the bank is "by low and sell high". This indicates the said bank would pay lesser amount of rupees when dollars are purchased and take more rupees, while selling the same.

Bid And Offered Rates or 2-Way Rates : Banks quote 2 FC rates. One of these is the rate at which bank is ready to buy (bid rate) andthe other is the rate at which bank is ready to sell (offered rate). In quotation for USD = 43.20/30, the first part (43.20) is the purchase rate of the bank and the 2nd part (43.30) is the selling rate. .

Card Rates: Card rates are calculated at the beginning of each day, based on the current rates in the inter-bank market and cross ratesin the international market. The rates are quoted by the authorized dealers to the clients for various currencies for different kinds of transactions i.e. buying and selling of cheques, drafts etc From spot rates and forward margins in various currencies, the banks able to calculate the rates which are conveyed to branches.

Cross Rates : When rate for a particular currency is not available, it can be calculated through another common currency, which iscalled cross rate mechanism.
For example USD/INR rate is Rs.46.00/10 and GBP/USD is 1.6000/10. The GBP/INR rate shall be 73.6000/8061 (calculated as 46 x 1.60
13. 73.60 and 46.10 x 1.6010 = 73.8061).

EXCHANGE RATE QUOTATIONS

Exchange quotations come under two categories i.e. direct quotation and indirect quotation. In India, wef August 2, 1993, the system prevalent is of direct quotation.

DIRECT QUOTATION: FC is expressed as fixed unit and home currency in variable unit. Example - 1 US $ =
Rs.49.10.With a view to make profit, the rule to be followed for this quotation is buy low and sell high.
INDIRECT QUOTATION: FC is expressed in variable quantity and home currency in fixed unit. Example - Rs.ioo = USD 1.52.
To make profit, the rule followed for this quotation is buy high and sell low.

SPOT TRANSACTIONS & FORWARD TRANSACTIONS

In a contract, the actual payment in rupees and receipt in FC (say US $) may take place on the same day, two days later or a month later or more.

Value dating : While quoting the rates, the banks take into account the time factor i.e. how much time is going to be taken to get thepurchased currency credited to the NOSTRO account abroad. This date is known as value date. There are 3 time frames for this i.e. cash value, torn value and spot value.

Cash Value: When the payment in rupees and receipt in US $ takes place on the same day, it is called a cash transaction or value today.

Tom value and spot value: When the payment is rupees and receipt in US $ takes place after some time (due to timeinvolved in administration of the transaction) it may be tom rate (where deal is settled on the immediately succeeding working day) and spot transaction when it is settled within next 2 days.

Date of Contract	Delivery Date / settlement date	Rate to be used
Oct 12, 2017	Oct 12, 2017	Cash/ Ready Rate
Oct 12, 2017	Oct 13, 2017	Tom Rate
Oct 12, 2017	Oct 14, 2017	TT or Spot Rate
Oct 12, 2017	Dec 12, 2017	Forward

Forward transaction: When the payment in rupees and receipt in US $ takes place on some predetermined future day after next 2days, it is called a forward transaction.

A forward contract for delivery two months means the exchange of currencies shall be completed after two months from date of contract.

Premium or discount on forward transactions: The forward rate of a currency is normally either costlier or cheaper than itsspot rate. The difference between the spot rate and forward rate is called forward margin or swap points. When the forward margin is at premium the forward rate will be higher/costlier than the spot rate. Similarly, if the forward margin is at a discount, the forward rate shall be lower or cheaper than the spot rate.

Under a **direct quotation, the premium** is added to the spot rate for reaching the forward rate and discount is deducted from the spot rate to arrive at the forward rate.

Example : Spot price is USD = Rs.5o.10 / 50.20. 3 months premium is 51/55 paise. This means that 3 months USD forward would bequoted at 50.61 / 50.75. In this case USD is at a premium and Indian Rupee is at a discount.

Factors determining premium and discount : (a) rate of interest prevailing at home centre and the concerned foreign currency centre — currency earning higher ROT will be at a discount, (b) demand and supply position of the FC, (c) speculation about spot rates and
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Tom value and spot value: When the payment is rupees and receipt in US $ takes place after some time (due to timeinvolved in administration of the transaction) it may be tom rate (where deal is settled on the immediately succeeding working day) and spot transaction when it is settled within next 2 days.

Date of Contract	Delivery Date / settlement date	Rate to be used
Oct 12, 2017	Oct 12, 2017	Cash/ Ready Rate
Oct 12, 2017	Oct 13, 2017	Tom Rate
Oct 12, 2017	Oct 14, 2017	TT or Spot Rate
Oct 12, 2017	Dec 12, 2017	Forward

Forward transaction: When the payment in rupees and receipt in US $ takes place on some predetermined future day after next 2days, it is called a forward transaction.

A forward contract for delivery two months means the exchange of currencies shall be completed after two months from date of contract.

Premium or discount on forward transactions: The forward rate of a currency is normally either costlier or cheaper than itsspot rate. The difference between the spot rate and forward rate is called forward margin or swap points. When the forward margin is at premium the forward rate will be higher/costlier than the spot rate. Similarly, if the forward margin is at a discount, the forward rate shall be lower or cheaper than the spot rate.

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Factors determining premium and discount : (a) rate of interest prevailing at home centre and the concerned foreign currency centre — currency earning higher ROT will be at a discount, (b) demand and supply position of the FC, (c) speculation about spot rates and (d) exchange control regulations.

Summary of Exchange Rate Application

Rate	Transaction
TT Selling Rate	When handling of documents by the bank are not involved. It is calculated on the basis of interbank selling rate by adding exchange margin. It will be applied for All clean outward remittances such as DD,TC etc Cancellation of purchase such as bills purchased, returned unpaid Cancellation of clean inward remittances Cancellation forward purchase contract Outward remittance against import documents received

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	directly by the importers.
Bill Selling Rate	When transactions involve handling of documents such as payment for import documents, bill selling rate is applied. Retirement of import bills even if proceeds of these bills are by way of DD or TT. Crystallization of Documentary Import Bills.
TC/Currency selling rate	For selling of Travellers cheque or foreign currency.
TT Buying rate	It is calculated after deducting exchange margin from Inter-bank buying rate. For example; Cancellation of outward TT, MT etc Clean inward remittances where cover funds are already received from abroad Conversion of proceeds of instruments that are sent for collection

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TC/ Currency buying rate	For travelers cheque and currency buying.

EXCHANGE ARITHMETIC-

Calculation of FC rates requires high degree of accuracy as the errors can result into substantial loss of revenue. There are certain basic terms in the process which need to be understood properly;

Chain Rule : The fixing of rate of exchange between the foreign currency and Indian rupee through the some other currency, where direct relationship is not available, is done by a method known as 'chain rule'. The rate thus obtained is the 'cross rate' between these currencies.

Per Cent and per Mille : The per cent is proportion of per hundred. 2% is two parts in each 100 parts. A per mille is proportion of per 1000. 2 per mille means 2 parts in each Rs.1000.

Value date : It is the date on which a payment of funds or entry to an account actually becomes effective. *Example :* In case of Telegraphic transfer it become effective same day i.e. the delivery of both currency takes place same day.

Arbitrage : It means simultaneous sale and purchase of a currency in two different markets at different rates to make trading profits (by purchasing at lower and selling at higher price). If it involves only 2 markets (centres) it is called *simple arbitrage.* If it involves more than 2 markets it is called *compound arbitrage.*

DEALING ROOMS OPERATIONS IN IN FOREIGN EXCHANGE

The Dealers in foreign exchange are actually involved in buying and selling of various currencies and undertaking certain other related activities. The dealing room functions as a *profit centre.* There are 3 types of offices (i) Front Office (2) Back Office and (3) Mid office. 1. Front Office: The dealer maintains 2 types of positions (1) funds position and (2) currency position.

The funds position comprises inflow and outflow of funds. A mismatch could create the interest rate risk position in the form of interest payment in NOSTRO account or loss of interest income for the credit balance. The currency position emerges on sale or purchase of various currencies in merchant or inter-bank transactions. The open position can expose the dealer to a FC rate fluctuation risk. The dealer is required to operate within the positions fixed by the bank for this purpose.

The FC position takes into account all components of forex such as (a) mirror account of the currency (b) foreign currency notes (c) import suspense account (d) spot and forward positions.

"2. Back-office : Back office within the dealing room, takes care of processing of deals, reconciliation and accounts.

p Mid-office : Within dealing room, it deals with the risk management and fixation of risk parameters for dealing room operations. It an independent function.

Valuation of forex profit/loss : RBI has approved the guidelines on Uniform Standard Accounting Practices for valuation of forex profits / losses by ADs, which are issued by FEDAI. According to these guidelines, the banks are to undertake valuation at end of each month.

Management & control of dealing room and Risk Management in Foreign Exchange

As per RBI directives, the banks are required to frame their own guidelines for this purpose including fixation of suitable limits for open positions.

Different kinds of risks leading to Foreign Exchange Risk

Classification of Persons Authorised to deal in Foreign Exchange : Under FEMA, 1999, RBI prescribes guidelines for authorised dealers and other persons while handling forex transactions. RBI issues licences to banks & financial institutions. RBI also authorises no. of established firms, companies, hotels etc. to deal in foreign currency. They are called Money Changers.Those entities which can buy and sell FC notes, coins, Travellers' cheques are called Full fledged Money Changers and those authorised to buy only, are called Restricted Money Changers. As per RBI's guidelines issued in 2005, ADs and MCs are called Authorised persons, which are divided into following categories:

p AD Category-I (comprising Commercial, State & Urban Coop Banks)- All current and capital account transactions according to RBI directions issued from time-to-time. (No Change).

q Authorised Dealers Category-II (Upgraded FFMCs, Coop Banks, RRBs and others): Specified non-trade related current account transactions as at paragraph 3 below as also all the activities permitted to Full Fledged Money Changers. Any other activity as decided by the Reserve Bank.

r Authorised Dealers Category-III (Select Financial and other Institutions) Transactions incidental to the foreign exchange activities undertaken by these institutions.

s Full Fledged Money Changers (FFMCs) (comprising Dept. of Posts , Urban Co-op. Banks and other FFMCs)

FOREIGN EXCHANGE DEALERS' ASSOCIATION OF INDIA (FEDAI)

FEDAI is a non-profit making body promoted in 1958 with RBI's approval. ADs are its members. It prescribes guidelines and rules for market operations. RBI guidelines for ADs in respect of operations and risk management of their owns assets and liabilities that can be offered to clients

p AD Category I banks may open/close Rupee accounts (non-interest bearing) in the names of their overseas branches or correspondents without prior reference to the Reserve Bank. Opening of Rupee accounts in the names of branches of Pakistani banks operating outside Pakistan requires specific approval of the Reserve Bank.

2.Funding of Accounts of Non-resident Banks : AD Category I banks may freely purchase foreign currency from their overseas correspondents/branches at on-going market rates to lay down funds in their accounts for meeting their bonafide needs in India.
3.Overdrafts / Loans to Overseas Branches/ Correspondents : AD Category I banks may permit their overseas branches/ correspondents temporary overdrawals not exceeding Rs.500 lakhs in aggregate, for meeting normal business requirements. This limit applies to the amount outstanding against all overseas branches and correspondents in the books of all the branches of the authorised AD Category I bank in India. This facility should not be used to postpone funding of accounts. If overdrafts in excess of the above limit are not adjusted within five days a report should be submitted to RBI within 15 days from the close of the month, stating the reasons thereof. Such a report is not necessary if arrangements exist for value dating.
4.Rupee Accounts of Exchange Houses : Opening of Rupee accounts in the names of Exchange Houses for facilitating private remittances into India requires approval of the Reserve Bank. Remittances through Exchange Houses for financing trade transactions are permitted upto Rs.5,00,000 per transaction.
5.Investments: AD Category I banks are free to undertake investments in overseas markets up to the limits approved by their Board. Such investments may be made in overseas money market instruments and/or debt instruments issued by a foreign state with a residual maturity of less than one year and rated at least as AA (-) by Standard & Poor / FITCH IBCA or Aa3 by Moody's. For the purpose of investments in debt instruments other than the money market instruments of any foreign state, bank's Board may lay down country ratings and country - wise limits separately wherever necessary.
p Use of FCNR-B balances : AD Category I banks may also invest the un-deployed FCNR (B) funds in overseas markets in long-termfixed income securities subject to the condition that the maturity of the securities invested in do not exceed the maturity of the underlying FCNR (B) deposits.
q **Surplus in NOSTRO accounts:** Foreign currency funds representing surpluses in the NOSTRO accounts may be utilised for:making loans to resident constituents for meeting their foreign exchange requirements or for the Rupee working capital/capital expenditure needs of exporters/ corporates who have a natural hedge or a risk management policy for managing the exchange risk subject to the prudential/interest-rate norms, credit discipline and credit monitoring guidelines in force.
extending credit facilities to Indian wholly owned subsidiaries/ joint ventures abroad in which at least 51 per cent equity is held by a resident company, subject to the guidelines issued by Reserve Bank (Department of Banking Operations & Development).
r Loans/Overdrafts : All categories of overseas foreign currency borrowings of AD Category I banks, (except for borrowings at (c) below), 'including existing External Commercial Borrowings and loans/overdrafts from their Head Office, overseas branches and correspondents and overdrafts in NOSTRO accounts (not adjusted within five days), shall not exceed **100** per cent of their unimpaired Tier I capital or USD 10 million (or its equivalent), whichever is higher. The aforesaid limit applies to the aggregate amount availed of by all the offices and branches in India from all their branches/correspondents abroad and also includes overseas borrowings in gold for funding domestic gold loans. If drawals in excess of the above limit are not adjusted within five days, a report, should be submitted to Reserve Bank of India, within 15 days from the close of the month
s Small and Medium Enterprises (SMEs) having direct and / or indirect exposures to foreign exchange risk can book / cancel / /roll over forward contracts without production of underlying documents to manage their exposures effectively
t Resident individual to hedge their foreign exchange exposures arising out of actual or anticipated remittances, both inward andoutward, can book forward contracts, without production of underlying documents, up to a limit of USD 10,00,0o0 (Oct 2015), based on self declaration. The contracts may be permitted to be booked up to tenors of one year only.
AD Category I banks may also allow **importers and exporters to book forward contracts** on the basis of a declaration of an exposure and based on past performance up to the average of the previous three financial years' (April to March) actual import/export turnover or the previous year's actual import/export turnover, whichever is higher

1. BASICS OF FOREX DERIVATIVES

Any activity you indulge in is associated with uncertainty which may result in some loss or some gain. In financial parlance, risk is associated with a loss that is expected to be incurred due to happening or non happening of certain events. It is an unplanned event with financial consequences resulting in loss or reduced earnings. The risk could be more or less depending upon the area of operation, volume, number of players, etc. The arena of international trade and foreign exchange operations is also prone to risks, mainly due to the complex nature of transactions, the individual characteristics of different currencies as also a vast area of operations. Like in any other human activity, risk cannot be avoided in international trade and foreign exchange operations. While in the international trade buyer risk, seller risk, shipping risk, etc., keep the parties on vigil, the foreign exchange operations arp plagued with exchange risk, settlement risk, liquidity risk, country risk, sovereign risk, interest rate risk, and operational risk. Risk and return have a direct relationship between them in as much as higher risks means higher returns. In the process of earning higher returns, one can enhance the risks beyond manageable levels. Therefore, risks needs to be accepted and managed effectively and efficiently to minimize the adverse effect and maximize the profit/goals of the organization.

RISKS IN INTERNATIONAL TRADE

Risk means probability of loss arising out of uncertainty about an event. An activity may turnout to be profitable and may

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result into loss also. The risk in a currency transactions or commodity transaction arises due to exposure undertaken by the bank concerned. The level of risk may be higher in case of international trade because it is surrounded by a no. of risks due to vast area of operation where the buyers and sellers are spread in different countries, the goods and value goods can more in opposite direction, there could be movement in the currency of the seller's and buyer's country.

Various kinds of risk involved in international trade include buyer risk, seller risk and shipping risk.

Buyer risk : The risk which a seller is exposed to and arises on account of buyer's non-acceptance of the goods / non-payment p delayed payment etc. The transaction is considered to be complete only when the buyer accepts the goods and seller gets the payment.

Seller risk : The risk that a buyer is exposed to and arises on account of non-shipment of goods by the seller OR delayed shipment OR shipment of poor quality of goods.

Shipping risk : The risk that buyer and seller are exposed to and arises on account of mishandling of goods, abandonment of goods, wrong delivery of goods, delivery of goods at another destination by the intermediary like shipping company, handling agent, port authorities etc.

Other risk : The buyer and seller can face other risks also in international trade that may include the settlement risk, competition risk, price risk, legal risk etc.

DIFFERENT KINDS OF RISKS RELATED TO FOREX TRANSACTIONS

Foreign exchange operations face large no. of different type of risk due to a variety of reasons such as location of forex markets without any single location, markets existing in different time zones, frequent fluctuations in the foreign currency rates, effect of policies of the government and central banks of the related country etc.

Foreign exchange exposure: The exposure can be classified into 3 categories:

p *Transaction exposure :* This arises on account of normal business operation. A transaction in foreign exchange canexposure a firm to currency risk, when compared to the value in home currency.

q *Translation exposure :* It arises on valuation of assts and liabilities created through foreign exchange and receivables orpayable in home currency, at the end of accounting period. These are notional and not actual.

r *Operating exposure :* These are the factor external to a firm such as change in competition, reduction in import duty,reduction in prices by other country exporters etc.

Exchange rate risk : Even the major currencies may experience substantial exchange rate movements over relatively short periods of time. These can alter the balance sheet of a bank if the bank has assets or liabilities domiciled in those currencies. An adverse movement of the rate can alter the value of the foreign exchange holdings, if not covered properly. The dealers have to cover the position immediately.

Positions in a foreign currency : When the assets and the outstanding contracts to purchase that currency are more than the liabilities plus and the outstanding contracts to sell that currency.

Long or overbought position : When the purchases (and outstanding contracts to purchase) are more than the sale (the outstanding contracts to sell).

Short position or oversold position : When the purchases (and outstanding contracts to purchase) are less than the sale (the outstanding contracts to sell).

Overbought or oversold position : It is called open position

Covering of position risk : The position is covered by fixing suitable limits (such as daylight position limit, overnight position limit,single deal limit, gap-for-ward mismatch limits).

Prudent limit prescribed by RBI for open position : RBI has given discretion to bank Boards to fix their own open position limitsaccording to their own requirement, expertise and other related considerations.

Pre-settlement risk : It is the risk of failure of the counter party, due to bankruptcy or closure or other risk, before maturity of thecontract. This may force the bank to cover the contract at the ongoing market rates resulting into loss due to difference prevailing between the contracted rate and rate at which the contract covered.

Settlement risk: Payment/delivery of one currency and received of other currency by both the parties. Settlement risk is therisk of failure of the counter party during the course of settlement due to time zone differences between the two currencies which are to be exchanged. For example, if a bank in the earlier time zone (say **in** Australia) performs its obligation and delivers the currency and a bank in a later time zone (say USA) fails to deliver or delivers with delay, the loss may be caused to the bank in the earlier time zone.

Foreign exchange settlement risk is also called temporal risk or Herstatt risk (named after failure of Bankhaus Herstatt in Germany)

The settlement risk can be taken care of by operating the system on a single time basis and also on real time gross settlement (RTGS) basis.

Liquidity risk: The liquidity risk is where a market does not have the capacity to handle, at least **without** significant adverseimpact on the price, the volume of whatever the borrower buys or sells at the time he want to deal. Inability to meet debt when they fall due could be another form of such risk.

For example, if there is deal of UK Pound purchase against the rupee and the party selling the UK Pound is short of pound in its NOSTRO account, it may default in payment or it may meet its commitment by borrowing at a very high cost.

Country risk: It is the risk that arises when a counter party abroad, is unable to fulfill its obligation due to reasons other than the

normal risk related to lending or investment.

For example, a counter party is willing and capable to meet its obligation but due to restrictions imposed by the govt. of the country or change in the polices of the govt., say on remittances etc. is unable to meet its repayment / remittance capacity. Country risk can be very high in case of those countries that are having foreign exchange reserve problem.

Banks control country risk by putting restrictions on overall exposure, country exposure.

Country risk is in addition to normal credit risk. While the normal credit risk is due to failure on meeting obligation on the part ofcounterparty on its own, the country risk arises due to actions initiated by the Govt. of that country due to which counterparty **is not** able to perform its part.

Sovereign risk : It is larger than country risk. It arises when the counterparty is a foreign govt. or its agency and enjoys sovereignimmunity under law of that country. **Due to** this reason, legal **action** cannot be taken against that counterparty. This risk can be reduced through disclaimers **and** by imposing 3'd country jurisdictions.

Interest rate risk: The potential cost of adverse movement of interest rates that the bank faces on its deposits and otherliabilities or currency swaps, forward contracts etc. is called interest rate risk. This risk arises on account of adverse movement of interest rates or due to interest rate differentials. The bank may face adverse cost on its deposit **or** adverse earning impact on its lending and investments due to such change in interest rates.

Interest rate can be managed by determining the interest rate scenario, undertaking appropriate sensitivity exercise to estimate the potential profit or losses based on interest rate projections.

Gap risk : Banks on certain occasions are not able to match their forward purchase and sales, borrowing and lending whichcreates a mismatch position, which is called gap risk. The gaps are required to be filled by paying or receiving the forward differential. These differentials are **the** function of interest rates.

The gap risk can be managed by using derivative products such as interest rate swaps, currency swaps, forward rate agreements.

Fledging risk: This occurs when one fails to achieve a satisfactory hedge for one's exposure, either because it could not be arranged or as the result of an error. One may also be exposed to basic risk where the available hedging instrument closely matches but does not exactly mirror or track the risk being hedged.

Operational risk : It is a potential catch that includes human errors or defalcations, loss of documents and records, ineffectivesystems or controls and security breaches, how often do one consider the disaster scenario.

Legal, jurisdiction, litigation and documentation risks including netting agreements and cross border insolvency. Which country'slaws regulate individual contracts and the arbitration of disputes ? Could a plaintiff take action against a borrower in an overseas court where they have better prospects of success or of higher awards ? There is a growing and widespread belief that, whatever goes wrong, someone else must pay. The compensation culture whatever its justification or cause, is becoming a big problem for many businesses.

RISK MANAGEMENT

For management of risk, the bank concerned has to frame a details policy, fix specific limit structure for various risks and operations, a sound management information system and specified control, monitoring and reporting process.

The process of risk management begins from the Board of Directors, which approves a policy for management of various types of risk which a bank may be exposed to.

The risk management policy of a bank should cover the goals and objectives, delegation of powers and responsibilities, activities to be undertaken, level of acceptable risk, authority to undertake such functions and system of review.

In India, RBI issued ICG i.e. Internal Control Guidelines for foreign exchange business covering dealing room operations, code of conduct for dealers, brokers, set up of the dealing room, back office and risk management structure.

According to these guidelines, the banks are required to fix limits on exposures as under:

Overnight limit : The maximum amount a bank can keep overnight when the markets in its time zone are closed.

Daylight limit : It is the maximum amount the bank can expose itself at any time during the day, for meeting the needs ofthe customers and also its own trading operations.

Gap limit : It is the maximum inter-period exposure that a bank can take.

Counter party limit : The maximum amount that a bank can expose itself to a particular party (called counterparty)

Country limit : It covers max exposure on a single country.

Dealer limit : This is the maximum amount that a dealer can keep exposed during the operating hours.

Stop loss limit : This is the maximum loss limit for adverse movement of rates.

Deal size limit : This is the maximum amount of size of a deal that can be made to restrict operational risk on large size deals.

Settlement risk : Maximum amount of exposure to any entity, maturing on a single day.

DERIVATIVES

In India, different derivatives instruments are permitted and regulated by various regulators, like Reserve Bank of India (RBI), Securities and Exchange Board of India (SEBI) and Forward Markets Commission (FMC). Broadly, RBI is empowered to regulate the interest rate derivatives, foreign currency derivatives and credit derivatives.

Definition : A derivative is a financial instrument:

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ii. whose value changes in response to the change in a specified interest rate, security price, commodity price, foreign exchange rate, index of prices or rates, a credit rating or credit index, or similar variable (sometimes called the 'underlying');

iii. that requires no initial net investment or little initial net investment relative to other types of contracts that have a similar response to changes in market conditions; and

iv. that is settled at a future date.

For regulatory purposes, derivatives have been defined in the Reserve Bank of India Act, as "an instrument, to be settled at afuture date, whose value is derived from change in interest rate, foreign exchange rate, credit rating or credit index, price of securities (also called "underlying"), or a combination of more than one of them and includes interest rate swaps, forward rate agreements, foreign currency swaps, foreign currency-rupee swaps, foreign currency options, foreign currency-rupee options or such other instruments as may be specified by the Bank from time to time.

Derivatives Markets

There are two *distinct groups* of derivative contracts:

Over-the-counter (OTC) derivatives: Contracts that are traded directly between two eligible parties, with or without the use of an intermediary and without going through an exchange.

Exchange-traded derivatives: Derivative products that are traded on an exchange.

Participants : Participants of this market can broadly be classified into two functional categories, namely, (a) users (who participates in the derivatives market to manage an underlying risk) and (b) the market-maker who provides continuous bid and offer prices to users and other market-makers. A market-maker need not have an underlying risk.

Purpose : Derivatives serve a useful risk-management purpose for both financial and nonfinancial firms. It enables transfer of various financial risks to entities who are more willing or better suited to take or manage them.

Users can undertake derivative transactions to hedge - specifically reduce or extinguish an existing identified risk on an ongoing basis during the life of the derivative transaction - or for transformation of risk exposure, as specifically permitted by RBI.

CORRESPONDENT BANKING AND NRI ACCOUNTS

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FOREIGN EXCHANGE MANAGEMENT ACT (FEMA)

The Foreign Exchange Management Act 1999 (FEMA) was enacted on December 02, 1999 to replace Foreign Exchange Regulation Act (FERA) 1973. The Act came into on June 01, 2000 and extends to the entire country, all branches, offices, agencies outside India - those owned or controlled by a person residing in India.

Objective of FEMA :(i) Facilitating external trade and payments and (ii) for promoting the orderly development and maintenance offoreign exchange market in India.

Authorised persons (APs)

All transactions can be carried by residents and non-residents through APs. An AP may be a dealer (Authorised Dealer of Category I, a)or Category III) or a money-changer. It may be an off-shore banking unit or any other person appointed under the Act. RBI issues licences to authorised person. It can revoke the authorisation if the person fails to comply with the conditions.

Classification of Persons Authorised to deal in Foreign Exchange

a AD Category-I (comprising Commercial, State & Urban Coop Banks) : All current and capital account transactions according to RBI directions issued from time-to-time.

b Authorised Dealers Category-II (Upgraded FFMCs, Coop Banks, RRBs and others):
Specified non-trade related current account transactions as at paragraph 3 below as also all the activities permitted to Full Fledged Money Changers. Any other activity as decided by RBI.

c Authorised Dealers Category-III (Select Financial and other Institutions): Transactions incidental to the foreign exchange activities undertaken by these institutions.

d Full Fledged Money Changers (FFMCs): (comprising Dept. of Posts , Urban Co-op. Banks and other FFMCs)

RBI powers under FEMA

RBI can prohibit, restrict and regulate various transactions such as transfer or issue of any foreign security by a resident of India and by a person residing outside India., borrowing or lending in foreign exchange, borrowing or lending in rupees between a resident in India and a person outside India, deposits between residents in India and residents outside India, export, import or holding of currency or currency notes, transfer of immovable property outside India other than a lease not exceeding five years, by a person resident in India, giving guarantee or surety in respect of any debt obligation or other liability incurred by person resident in Indian to a person outside India and vice-versa, etc.

CORRESPONDENT BANKING

Correspondent banking: It is relationship between two banks having mutual accounts with each other or one of them is havingaccount with other. OR a relationship and servicing of banking needs, as agent without having account relationship.

Benefit of correspondent banking: Through correspondent banking, a bank is able to handle business in another city or countrythrough local banks acting as agent. The system eliminates the need to have global network branches that involves high costs. Hence bank can take advantage of the business opportunities in other countries.

Functions handled by correspondent banks:

c) **account services** such as (a) clearing house functions, (b) collections, payments, (c) overdrafts, (d) loan facility and (e)investment services

d) **other services** such as (a) LC advising, (b) LC confirmation, (c) Bankers acceptances, (d) issue of guarantees, (e) forexservices, (f) custodial services etc.

Types of accounts opened under correspondent banking: These accounts include NOSTRO, VOSTRO, LORO accounts.

NOSTRO account: This is an account of a bank in another country (say SBI's account in New York with Citibank). This is called "ouraccount with you".

VOSTRO account: This is an account of a foreign bank in India. (say Citibank's account in New Delhi with SRI). This is called "youraccount with us".

LORO account: This is an account of a bank in another country which is used by a 3.[3]bank (say for BoB, SBI's account in New Yorkwith Citibank). This is called "Their account with them".

Mirror account: Mirror account is shadow (like a copy) of the NOSTRO account. The entries in this account are used forreconciliation purpose.

ELECTRONIC MODES OF TRANSMISSION / PAYMENT

SWIFT: SWIFT stands for Society for Worldwide Inter-bank Financial Telecommunication. It provides securedtelecommunication of financial messages amongst banks and financial institutions, throughout the world. Authentication of messages is done through bilateral key exchange. The cost of sending message is only 1/4th of the conventional talex system.

CHIPS: CHIPS stands for "Clearing House Inter-bank payment system'. It is a major payment system in USA, being used by majorbanks. **It** is operative in New York only.

Fedwire: This is a payment system operated by Federal Reserve Bank of US operated all over USA.

ABA number: It is the no. allotted by Federal Reserve of USA to banks participating in Fedwire, to identify the senders andreceivers of payment.

CHAPS: CHAPS, the Clearing House Automated Payments System is British equivalent to CHIPS, handling receipts and payments inLondon. It is used by a large no. of banks in UK.

Target: It stands for Trans-European Automated Real-time Gross Settlement Express Transfer system in EURO payment systemcomprising 15 national RTGS systems working in Europe.

RTGS-plus: RTGS plus is German hybrid clearing systems and operating as an European oriented RTGS and payment system.

EBA-EURO-1: It is a netting system with focus on cross border Euro payments.

RTGS in India: RBI implemented RTGS in India. It functions on line. Banks maintain a pool account with RBI for inflow andoutflow of funds through RTGS. Minimum amount is Rs.2 lac for RTGS.

NEFT in India: It is an electronic funds transfer system which functions on a batch basis. There are no amount ceilings.

Types of Persons : Non-Resident: As per FEMA, a person who is not a resident, is called a non-resident.

Person resident in India

(i) a person residing in India for more than one hundredand eighty-two days during the course of the preceding financial year but does not include

a person who has gone out of India or who stays outside India, in either case

c. for or on taking up employment outside India, or

d. for carrying on outside India a business or vocation outside India, or

e. for any other purpose, in such circumstances as would indicate his intention to stay outside India for an uncertain period;

a person who has come to or stay in India, in either case, otherwise than

for or on taking up employment in India, or

for carrying on in India a business or vocation in India, or

for any other purpose, in such circumstances as would indicate his intention to stay in India for an uncertain period;

b. any person or body corporate registered or incorporated in India,

c. 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;

Non-Resident Indian (NRI) : He is a person resident outside India who is a citizen of India. Indian students abroad, also treated NRIs.**Person of Indian Origin (PIO) :**A person resident outside India who is a citizen of any country other than Bangladesh or Pakistan and:

1. Who was a citizen of India by virtue of the Constitution of India or the Citizenship Act, 1955; or
2. Who belonged to a territory that became part of India after the 15th day of August, 1947; or
3. Who is a child or a grandchild or a great grandchild of a citizen of India or of a person referred to in clause (a) or (b); or

d) Who is a spouse of foreign origin of a citizen of India or spouse of foreign origin of a person referred to in clause (a) or (b) or (c)

Non

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Resident: As per section 2(v) of the FEMA 1999, a person is called resident in India if he stays in India for more than 182 days duringthe preceding financial year except those who have gone out of India for taking up employment outside India or for carrying on a business or vocation outside India or for any other purpose indicating his intention to stay abroad for indefinite period. **NON Resident**: Person resident outside India means a person who is not resident in India.

Person of Indian Origin: A. Person of Indian Origin is one who is presently not a national of Pakistan or Bangladesh and: (a) who at anytime held an Indian passport; or (b) he himself, either of his parents or any of his grandparents was a citizen of India by virtue of Constitution of India or the Citizenship Act,1955 ; or (c) the person is a spouse of Person of Indian Nationality / Origin.

Overseas Corporate Bodies are those in which at least 60% shareholding is of NRI. OCBs are not allowed to open NRI accounts.

Students who go abroad for studies have also been given the facility of opening NRI accounts.

Non-resident accounts are of 3 types (a) Non Resident ordinary (b) Non Resident (External) (c) Foreign Currency Non Resident (Bank) account. Salient features of these accounts are as under:

FEATURES OF NRI DEPOSITS Foreign Currency Non-Resident (Bank) Account (FCNR(B) A/c) — (w.e.f. 15.5.1993)

Account holder: NRI of Indian nationality or origin (RBI approval for Bangladesh entities/Pakistan entities and citizens).

Joint account: Can be of two or more NRIS. With close resident relatives, joint account (Former, or Survivor) can be opened. Relatives can operate a/c as power of attorney holder for local withdrawals or remittance abroad in name of account holder.

Currencies: Any freely convertible currency.

Type of account: FDR only (a) 1 year and above, less than 2 years (b) 2 years and above less than 3 years (c) 3 years and aboveless than 4 years (d) 4 years and above less than 5 years (e) 5 years only. RD, SB or CA is not allowed.

Repatriation: Principal and interest permitted.

Source of funds: Foreign Inward remittance (FIR) or transfer from NRE-RA account (at TT selling rate)

Interest rate and interest payment: Ceiling rate fixed by RBI (presently LIBOR + 2% (1 year to less than 3 years) and LIBOR + 3%(for 3 years to 5 years w.e.f. 01.03.14). No interest payment if cancellation before one year. For one year deposit,. no compounding of interest. For above one year, compounding on 180 days basis. Interest payment on 360 days in year basis. On floating ROI, half yearly reset is allowed.

Fund or non-fund Rupee loan: Up to value of FDR with proper margin to the depositor or 3rd party. Margin / interest rate bankdiscretion. Loans proceeds to be credited to NRO account. Loans can be repaid from FCNR, NRE or NRO account balances. Banks should not mark any type of lien, direct or indirect,

against these deposits. Premature payment not allowed if loan is granted. FC loan can be given in India or abroad.

Nomination facility is available.

Income Tax: Interest is not taxable. TDS not applicable.

Additional ROI not allowed to Staff (Jul 18, 2012)

At the request of the depositor, banks can permit remittance of the maturity proceeds to third parties outside India, providedbank is satisfied about the bonafides of the transaction.

Non-Resident External (Rupee Account)

Account holder: NRIs of Indian nationality or origin (RBI approval for Bangladesh entities/Pakistan citizens and entities).

Joint account: Can be in the names of two or more NRIs. With close resident relatives, joint account (Former or Survivor) can beopened. Relatives can operate a/c as power of attorney holder for local withdrawals or remittance abroad in name of account holder.

Currencies: Indian rupee by converting foreign currency.

Type of account: Current, saving or FDR. FDR period at discretion of banks.

Repatriation: Principal and interest permitted.

Source of funds: Foreign Inward remittance (FIR) or transfer from FCNR-B account (at 'TT buying rate) or transfer of repatriablefunds from NRO account

Interest rate and interest payment : Bank discretion but not more than domestic deposit (deregulated w.e.f. Dec 16, 2011).

Rupee loan: Same as in case of FCNR-B account.

Nomination facility is available.

Income Tax: Interest is not taxable. TDS not applicable.

Additional ROI not available to Staff w.e.f. Jul 18, 2012.

Important Notes (a) PoA holders cannot credit foreign currency notes and foreign traveller'schequesin NRE accounts. (b) Banksmay credit the proceeds of account payee cheques/ demand drafts / bankers' cheques, issued against encashment of foreign currency to the NRE account of the NRI account holder where the instruments issued to the NRE account holder are supported by encashment certificate issued by AD Category-I / Category-IL

Non-Resident Ordinary Account (NRO)

Account holder: NRIs or Person of Indian Origin (individuals & not entities from Bangladesh, can be allowed without RBIpermission w.e.f. 11.2.13 Pakistan citizen not to be allowed). Foreign students can also open NRO accounts (RBI 20.09.13).

Joint a/c : Allowed with resident individuals.

Currencies Indian rupee.

Account: Current, saving, RD or FDR. FDR 7 days to10 years.

Repatriation: Interest and current income is permitted. Remittance, including of sale proceeds of immovable property alsoallowed @ USD 1 million per financial year for bonafide purposes.

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Source of funds: New account can be opened with Foreign Inward remittance. Existing account of an NRI opened when he wasresident, will be designated as NRO by the bank.
Interest rate: Bank discretion. Not more than domestic deposit interest rates.
Nomination facility is available.
Income Tax: Interest is taxable. TDS provisions applicable for all interest payments (FD/SB account).
Transfer of repatriable amount from NRO to NRE permitted (May 8, 2012) within USD 1 million /FY subject to payment of tax,as applicable.
Additional ROI not allowed to Staff (Jul 18, 2012)
Rupee loan Up to value of FDR with proper margin to depositor or 3rd party. FC loan or loan abroad not permitted.

Power of attorney: The facility of operation of accounts by PA holder is permitted for local withdrawals or remittance abroad inname of account holder.

Accounts of Foreign Students in India

NRO account can be opened on the basis of passport, photo and admission letter, for KYC purpose. Local address proof to be provided within 30 days, when monthly withdrawal will be up to Rs.50000 and foreign inward remittance up to USD 1000. On receiving local address proof, normal operations can be allowed.

NRO Accounts Of Foreign Nationals of Non- Indian Origin on a visit to India

NRO (current/savings) a/c max 6 months. Source and use of funds: Funds remitted from outside India through banking channel or by sale of forex brought into India. All payments' to residents exceeding INR 50,000 by means of cheques / pay orders / demand drafts.

Remittance : The balance may be converted by AD bank into foreign currency for payment to the account holder at the time of his departure from India provided the account has been maintained for a period not exceeding 6 months and the account has not been credited with any local funds, other than interest accrued thereon. If account maintained for more than 6 months, account holder to seek permission on plain paper from Regional Office of RBI.

Accounts of Foreign nationals resident in India Foreign nationals resident in India can open and maintain a resident Rupee account in India in terms of Notification No.5/2000-RB dated May 3, 2000 viz., Foreign Exchange Management (Deposit) Regulations, 2000, as amended from time to time.

Accounts of residents Resident Foreign Currency Account (RFC)

Account holder: A resident in India who was earlier an NRI (at least one year stay abroad) and became resident again on or after 18.04.92

Source of funds: (a) Forex received as pension/ superannuation /other benefits from employer abroad (b) Realization of assets held abroad (c) Forex acquired as gift or inheritance from person who was NRI (d) Existing FCNR account or NRE-FD to be converted to RFC FD at discretion of account holder before or after maturity.
Joint account: It can be single account. With close resident relatives, joint account can be opened as FORMER or SURVIVOR account.
Type of account : Savings, Current, Fixed Deposit (min 7 days and max 10 years)
Repatriation is permitted.
Interest rates: The banks are free to determine ROI.
Use of funds: No restrictions

Resident Foreign Currency (Domestic) Account - RFC(D)

Account holder: Resident Individuals
Source of funds: Foreign exchange acquired, (a) while on a visit abroad (b) from any person on visit to India or honorarium or gift or for services or settlement of any lawful obligation (c) by way of honorarium or gift while on a visit abroad (d) representing unspent foreign exchange acquired during travel abroad. Amount to be converted in rupees, latest by last day of next month.
Type of account : Only current account
Interest : No interest payable on this deposit
Use of funds: For all permitted transactions.

Exchange Earner's Foreign Currency Account (EEFC Account)

Account holder : Exporters of goods and services, resident in India
Source of funds: Up to 100% of forex earnings can be kept in the account. But amount to be converted in rupees, latest by last day of next month.

Use of funds: Balance can be transferred to NRE/FCNR account on change of status from resident to non-resident. Funds can be used for adjustment of pre-shipment loans.
Loan: No loan can be allowed against the balances in such account.
Type of account: Current account, single or joint (FORMER or SURVIVOR) with close resident relatives.
Interest : No Interest is payable

LIBERALISED REMITTANCE SCHEME (LRS) FOR RESIDENT INDIVIDUALS

RBI introduced LRS on Feb 04, 2004. Major changes were made by RBI in LRS w.e.f. 01.06.2015 (based on Govt. notification 15.05.15).

Eligibility: All resident individuals including minors and non-individuals are eligible. Remittances under the facility can beconsolidated in respect of family members subject to individual family members complying with the terms and conditions.

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It is mandatory to have PAN number to make remittances beyond USD 25000.00 for current account transaction and for all capital account transactions.

Forex can be purchased from authorised person which indude AD Category-1 Banks, AD Category-2 and Full Fledged Money Changers.

Capital Accounts transactions Remittances up to USD 250,000 per financial year can be allowed for permissible capital accounttransactions as under: I) opening of foreign currency account abroad; ii) purchase of property abroad; iii) making investments abroad; iv) setting up Wholly owned subsidiaries and Joint Ventures abroad; v) loans including in Indian Rupees to Non-resident Indians relatives as defined in Companies Act, 2013.

Current account transactions: All facilities (Including private/business visits) for remittances have been subsumed under overalllimit of USD 250,000/FY.

Facilities for Individuals: Individuals can avail of forex facility for the following purposes within the limit of USD 250000.Additional remittance shall require prior approval of RBI. Private visits to a country (except Nepal & Bhutan),Gift or donation.

Going abroad for employment or immigration. Maintenance of close relatives abroad ,Travel for business, or attending a conference or specialized training or for meeting medical expenses, or check-up abroad, or for accompanying as attendant to a patient going abroad for medical treatment/ check-up. Expenses for medical treatment abroad , Studies abroad ,

Any other current account transaction

Exception: For immigration, medical treatment and studies abroad, the individual may avail of exchange facility in excess of LRS limit if required by a country of emigration, medical institute offering treatment or the university, respectively.

Facilities for persons other than individual: Donations up to 1% of forex earnings in previous 3 FY or USD 5,000,000, whichever is less, for: creation of Chairs in reputed educational institutes, contribution to funds (not being an investment fund) promoted by educational institutes; and technical institution/body/ association in the field of activity of the donor Company.

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.

Remittances exceeding USD 10,000,000 per project for any consultancy services for infrastructure projects and USD 1,000,000 per project, for other consultancy services procured from outside India.

Remittances exceeding 5% 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.

Loan facility: Banks **should not extend** any kind of credit facilities to resident individuals to facilitate remittances under theScheme.

Remittances not available under the scheme:

Remittance for any purpose specifically prohibited under Schedule-I (like purchase of lottery/sweep stakes, tickets, prescribed magazines etc.) or item restricted under Schedule II of FEMA (Current A/c Transactions) Rules, 2000.

Remittances made to Bhutan, Nepal, Mauritius or Pakistan.

Remittances made to countries identified by the Financial Action Task Force (FATF) as "non cooperative countries and territories" as available on FATF website (viz Cook Islands, Egypt, Guatemala, Indonesia, Myanmar, Nauru, Nigeria, Philippines and Ukraine) or as notified by RBI.

Remittances to individuals and entities identified as posing significant risk of committing acts of terrorism as advised separately by RBI to the banks.

Reporting of the transactions: The remittances made will be reported in the R-Return in the normal course.

Rules related to release / remittance of foreign exchange to residents

AD banks can release forex to residents in India as per Rules framed u/s Sec 5 of FEMA. Forex cannot be released for Schedule I transactions. For Schedule II transactions, Govt. permission is required. For Schedule III transactions, forex can be released up to specified limit by AD banks. Beyond that limit, approval of RBI is required.

Nepal & Bhutan - Forex for any kind of travel to or for any transaction with persons resident in Nepal and Bhutan cannot be released. Any amount of Indian currency can be used. Highest denomination of currency note can be Rs.100.
Up to Rs.25000, any denomination is allowed.

Form of foreign currency: 1. Coins, currency notes and traveller's cheques. Currency notes/coins can be up to US$ 3000. Thebalance can be traveller's cheque or banker's draft.

For Iraq and Libya currency notes and coins can be obtained up to US$ 5000 or its equivalent.

For Iran, Russian Federation, and other Republics of Commonwealth of Independent Countries, no ceiling.

Mode of purchase: In cash up to Rs.50, 000/-. Above this, payment by way of a crossed cheque/banker's cheque/payorder/demand draft / debit card / credit card only.

Surrender of unused forex: Currency notes and travellers' cheques within 180 days of return.

Retention of unused forex : US$2,000 or its equivalent. There is no restriction on residents for holding foreign currency coins.

Use of International Credit Card (ICC): Use of the ICCs / ATMs/ Debit Cards can be made for personal payments and for travelabroad for various purposes, only up to specified limits.

Export / Import of Indian currency by Residents or non-residents: Up to Rs. 25000 each to or from any country other thanNepal or Bhutan (Pakistan & Bangladesh Rs.10000) .

Import of Foreign exchange from abroad: Any amount subject to declaration on CDF.

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Mandatory CDF: Where total amount exceeds US$ 10,000 (or its equivalent) and/or value of foreign currency notes exceedsUS$ 5,000, declaration should be made to the Customs Authorities through Currency Declaration Form (CDF), on arrival in India.

Application for purchase of FC: Form A2. It is not required up to $ 25000. A2 to be preserved by banks for one year for verification by Auditors. endorsement on Passport : It is not mandatory for Authorised

Dealers to endorse the amount of foreign exchange sold for travel abroad on the passport of the traveller. However, if requested by the traveller, AD may record under its stamp, date and signature, details of foreign exchange sold for travel.

DOCUMENTARY LETTERS OF CREDIT

A Letter of Credit/Documentary Credit is a very common and familiar instrument, used for trade settlements across the globe. It is a link between buyers and sellers, reinforcing the buyer's integrity by adding to it, his banker's undertaking to pay, while sellers need to make shipments of goods specified and present shipping documents to banks, before getting the payment. Thus, for international trade, where buyers and sellers are far apart in two different countries, or even continents, the letter of credit acts as a most convenient instrument, giving assurance to the sellers of goods for payment and to the buyers for shipping documents, as called for under the credit.

In order to bring uniformity in matters pertaining to letters of credit documents and transactions, International Chambers of Commerce (ICC), *established in 1919 and headquartered in Paris, has framed uniform rules and procedures for issuance and handlingof transactions under letters of credit,* so that parties to letters of credit transactions uniformly interpret various terms and arebound by a common rule. These rules and procedures are called *Uniform Customs and Practices for Documentary Credits (UCPDC).* The UCPDC was first brought out in 1933, and has been revised from time to time in 1951, 1962, 1974, 1983, 1993 with the last revision in 2007. The current update of UCPDC is the publication No. 600 of ICC, which has been implemented with effect from 1.7.2007.

DEFINITION OF LETTER OF CREDIT

A documentary credit or/and letter of credit, (DC or LC) can be defined as a signed or an authenticated instrument issued by the buyer's banker, embodying an undertaking to pay to the seller a certain amount of money, upon presentation of documents, evidencing shipment of goods, as specified, and compliance of other terms and conditions.

An LC can also be defined as an undertaking issued by the bank, on behalf of the importer or the buyer, in favour of the exporter or the seller, that, if the specified documents, showing that a shipment has taken place, or a service has been supplied, are presented to *the issuing bank or its nominated bank,* within the stipulated time, *the exporter/seller* will be paid *the amount specified.*

Thus, in an LC transaction, following parties are involved:

9. The buyers/importers or the applicant — **on whose behalf LC is opened,**
10. The sellers/exporters or the **beneficiary of the LC,**
11. The opening bank (buyers bank), **who establishes the LC**
12. The advising bank (bank in sellers country), **who acts as an agent of the issuing bank and authenticates the LC.**
13. The confirming bank — **who undertakes to pay on behalf of the issuing bank,**
14. The negotiating bank (sellers bank or bank nominated by the opening bank),
15. Reimbursing bank — **who reimburses the negotiating or confirming bank.**

The advising bank, confirming bank and the negotiating bank could be the same

Operation of letter of credit

1. Buyer and seller enters into a contract for sale of goods or providing of services. The transaction is covered by LC.
2. On request of the buyer i.e. applicant, LC is issued by Opening Bank in favour of Beneficiary and sent to advising bank instead of sending directly to beneficiary.
3. After authentication of LC, the advising bank sends the LC to beneficiary.
4. After receiving LC, the beneficiary manufacturers the goods and makes shipment and prepares documents, as mentioned in LC.

5. Documents are presented by beneficiary to nominated bank for negotiation. Negotiating bank makes payment against these documents and claims payment on due date from opening bank.
2. Opening bank makes payment to negotiating bank and recovers the payment from applicant.

TYPES OF LETTERS OF CREDITS

Documents against Payment LC or Sight LC	DP LCs or Sight LCs are those where the payment is made against documents on presentation. (DA = Documents against payment, DP=Documents against acceptance)

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Documen ts a gai nst acceptance or us ance	DA LCs or Acceptance LCs are those, where the payment is to be made on the maturity date in terms of the credit. The documents of title to goods are delivered to applicant merely on acceptance of documents for payment. (DA = Documents against payment, DP=Documents against acceptance)
Deferred Payment LC	It is similar to Usance LC but there is no bill of exchange or draft. It is payable on a future date if documents as per LC are submitted.
I rrevocabl e and revocable credits	The issuing bank can amend or cancel the undertaking if the beneficiary consents. A revocable credit is one that can be cancelled or amended at any time without the prior knowledge of the seller. If the negotiating bank makes a payment to the seller prior to receiving notice of cancellation or amendment, the issuing bank must honour the liability.
Wi t h or w ith ou t r e-c ou rse	Where the beneficiary holds himself liable to the holder of the bill if dishonoured, is considered to be with-recourse. Where he does not hold Himself liable, the credit is said to be without-recourse. *As per RBI directive dated Jan 23, 2003, banks should not open LCs and purchase / discount / negotiate bills bearing the 'without recourse' clause.*
Restricted LCs	A restricted LC is one wherein a specified bank is designated to pay, accept or negotiate.
Confirmed Credits	A credit to which the advising or other hank at the request of the issuing bank adds confirmation that payment will be made. By such additions, the confirming bank steps into the shoes of the issuing bank and thus the confirming bank negotiates documents if tendered by the beneficiary.
Transferable Credits	The beneficiary is entitled to request the paying, accepting or negotiating bank to make available in whole or part, the credit Cu one or more other parties (Article 48 of UCPDC). For partial transfer to one or more second beneficiary/ies the credit must provide for partial shipment.
Back to back credits	A back to back credit is one where an exporter received a documentary credit opened by a buyer in his favour. He tenders the same to the bank in his country as a cover for opening another LC in favour of his local suppliers. The terms of such credit would be identical except that the price may be lower and validity earlier.
Red Clause Credits	A red clause credit also referred to a packing or anticipatory credit has a clause permitting the correspondent bank in the exporter's country to grant advance to beneficiary at issuing bank's responsibility. These advances are adjusted from proceeds of the bills negotiated.

	could be Airway Bill or Postal or courier receipt.
Insurance documents	The despatched goods are required to be insured for transit period. Insurance policy or insurance certificate should be signed by the company or underwriter or their agent. Amount, kinds of risk etc. should be same as mentioned in the letter of credit.

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Other documents	The letter of credit may also specify other documents to be presented along with the above documents which may include certificate of origin, certificate from health authorities etc.

DIFFERENT TYPES KINDS OF BILL OF LADING

Received for shipment Bill of lading: It is an acknowledgment that the goods have been received by the ship owners for shipment. It is not considered safe document for negotiation.

On-board Bill of lading : It acknowledges that the goods have been put on board of the shipment. This is considered safe for negotiation purpose.

Short form bill of lading : Where the terms and conditions of carriage are not printed on the bill of lading and a reference to another document containing terms and conditions is made on the bill.

Long form bill of lading : Where all terms and conditions of carriage are given on the document itself.

Clean bill of lading : Which bears no superimposed clause or notation that expressly declares the defective condition of goods or packaging. This is considered safe for negotiation purpose.

Claused bill of lading : Which bears superimposed clause or notation that expressly declares the defective condition of goods or packaging. Ship owner can disclaim his liability on loss to goods in case of such BL. Hence it is not considered safe.

Through Bill of lading : That covers the entire voyage covering several modes of transport. There is no guarantee of the carriers for safe carriage of goods.

Straight bill of lading BL that is issued directly in the name of the consignee, where the goods will be delivered to the consignee.

Chartered party bill of lading : Issued to a Chartered party who has hired the space in the vessel. **Liability of Issuing Bank**

As per UCPDC, an irrevocable Credit constitutes an definite undertaking of the Issuing Bank. Hence:

7. if the Credit provides for sight payment — to pay at sight,
8. if the Credit provides for deferred payment — to pay on the maturity date(s) determinable in accordance with the stipulations of the Credit,
9. if the Credit provides for acceptance to accept Draft(s) drawn by the Beneficiary on the Issuing Bank and pay at maturity, or
10. if the Credit provides for negotiation — to pay without recourse to drawers and/or bona fide holders, Draft(s) drawn by the Beneficiary and/or document(s) presented under the Credit. A Credit should not be issued available by Draft(s) on the Applicant. The Credit nevertheless calls for Draft(s) on the Applicant, banks will consider such Draft(s) as an additional document(s).

Advising Bank's Liability

As per UCPDC, a credit may be advised to a Beneficiary through another bank (the 'Advising Bank') without engagement on the part of the Advising Bank. If that bank, elects to advise the Credit, shall take reasonable care to check the apparent authenticity of the Credit which it advises. If the bank elects not to advise the Credit, it must so inform the Issuing Bank without delay. If the Advising Bank cannot 'establish such apparent authenticity it must inform, without delay, the bank from which the instructions appear to have been received that it has been unable to establish the authenticity of the Credit and if it elects nonetheless to advise the Credit it must inform the Beneficiary that it has not been able to establish the authenticity of the Credit.

Liability of the Confirming Bank

A confirmation of an Irrevocable Credit by another hank (the 'Confirming Bank') upon the authorisation or request of the Issuing Bank, constitutes a definite undertaking of the Confirming Bank, in addition to that of the Issuing Bank. Hence:

1. if the Credit provides for sight payment — to pay at sight,
2. if the Credit provides for deferred payment — to pay on the maturity date(s) determinable in accordance with stipulations of the Credit.
3. if the Credit provides for acceptance to accept Draft(s) drawn by the Beneficiary on the Confirming Bank and pay them at maturity,
4. if the Credit provides for negotiation — to negotiate without recourse to drawers and/or bona fide holders, Draft(s) drawn by the Beneficiary and/or document(s) presented under the Credit. A Credit should not be issued available by Draft(s) on the Applicant. If the Credit nevertheless calls for Draft(s on the Applicant, banks will Consider such Draft(s) as an additional document(s).

Examination of Documents

As per UCPDC, a Banks must examine all documents stipulated in the Credit with reasonable care to ascertain whether or not they appear, on their face, to be in compliance with the terms and conditions of the Credit. Documents, which appear on their face to be inconsistent with one another, will be considered as not appearing on their face to be in compliance with the terms and conditions of the Credit. Documents not stipulated in the Credit will not be examined by banks. If they receive such documents, they shall return them to the presenter or pass them on without responsibility.

Time for scrutiny of documents: The Issuing Bank, the Confirming Bank, if any, or a Nominated Bank acting on their behalf, shalleach have a reasonable time, *not to exceed 5 banking days* following the day of receipt of the documents, to examine the documents and determine whether to take up or refuse the documents and to inform the party from which it received the documents accordingly.

Insurance Documents

As per UCPDC, the:

A Insurance documents must appear on their face to be issued and signed by insurance companies or underwriters or theiragents.

B If the insurance document indicates that it has been issued in more than one original, all the originals must be presented unlessotherwise authorised in the Credit.

C Cover notes issued by brokers will not be accepted, unless specifically authorised in the Credit.

D Unless otherwise stipulated in the Credit, banks will accept an insurance certificate or a declaration under an open cover pre-signed by insurance companies or underwriters or their agents. If a Credit specifically calls for an insurance certificate or a declaration under an open cover, banks will accept, in
lieu of thereof, an insurance policy.

E Unless otherwise stipulated in the Credit, or unless it appears from the insurance document that the cover is effective at the latest from the date of loading on board or dispatch or taking in charge of the goods, banks will not accept an insurance document which bears a date of issuance later than the date of loading on board or dispatch or taking in charge as indicated in such transport document.

F: i. Unless otherwise stipulated in the Credit, the insurance document must be expressed in the same currency as the Credit.

4. Unless otherwise stipulated in the Credit, the minimum amount for which the insurance document must indicate the insurance cover to have been effected is the CIF (cost insurance and freight (...'named port of destination')) or CIP
(carriage and insurance paid to (...'named place of destination')) value of the goods, as the case may be, plus 10%, but only when the CIF or CIP value can be determined from the documents on their face. Otherwise, banks will accept as such minimum amount 110% of the amount for which payment, acceptance or negotiation is requested under the Credit, or 110% of the gross amount of the invoice, whichever is the greater.

Commercial Invoices

As per UCPDC:

A Unless otherwise stipulated in the Credit, commercial invoices

1. must appear on their face to be issued by the Beneficiary named in the Credit, and
2. must be made out in the name of the Applicant, and
3. need not be signed.

B Unless otherwise stipulated in the Credit, banks may refuse commercial invoices issued or amounts in excess of the amount permitted by the Credit. Nevertheless, if a bank authorised to pay, incur a deferred payment undertaking, accept Draft(s), or negotiate under a Credit accepts such invoices, its decision will be binding upon all parties, provided that such bank has not paid, incurred a deferred payment undertaking, accepted Draft(s) or negotiated for an amount in excess of that permitted by the Credit.

C The description of the goods in the commercial invoice must correspond with the description in the Credit. In all other documents, the goods may be described in general terms not inconsistent with the description of the goods in the Credit.

Bank-to-Bank Reimbursement Arrangements as per UCPDC

As per UCPDC: A If an Issuing Bank intends that the reimbursement to which a paying, accepting or negotiating bank is entitled, shallbe obtained by such bank (the 'Claiming Bank'), claiming on another party (the `Reimbursing Bank'), it shall provide such Reimbursing Bank in good time with the proper instructions or authorisation to honour such reimbursement claims.

B Issuing Banks shall not require a Claiming Bank to supply a certificate of compliance with the terms and conditions of the Credit to the Reimbursing Bank.

C An Issuing Bank shall not be relieved from any of its obligations to provide reimbursement if and when reimbursement is not received by the Claiming Bank from the Reimbursing Bank.

D The Issuing Bank shall be responsible to the Claiming Bank for any loss of interest if reimbursement is not provided by the Reimbursement Bank on first demand, or as otherwise specified in the Credit, or mutually agreed, as the case may be.

E The Reimbursing Bank's charges should be for the account of the Issuing Bank. However, in cases where the charges are for the account of another party, it is the responsibility of the Issuing Bank to so indicate in the Original Credit and in the reimbursement authorisation. In cases where the Reimbursing Bank's charges are for the account of another party they shall be collected from the Claiming Bank when the Credit is drawn under. In cases where the Credit is not drawn under, the Reimbursing Bank's charges remain the obligation of the Issuing Bank.

UNIFORM CUSTOMS AND PRACTICES FOR DOCUMENTARY CREDITS UCPDC-600

Uniform Customs and Practices for Documentary Credits - 600 (referred to as UCP-600), prepared by
ICC, Paris by revising the UCPDC-500, is being implemented wef July 01, 2007. It is 6th revision of
the Rules since first promulgation in 1933. The new document has 39 Articles (against 49 of UCPDC500) with supplement for Electronic Presentation covering 12 eArticles. UCPDC-600, shall be applicable to LCs that expressly indicate that these are subject to UCPDC-600.

ARTICLES OF UCPDC-boo