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The Legality of Forex Trading in India

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The legality of forex trading is one of the most controversial and argumentative topics in India. The term Forex comes from the word Foreign Exchange Market, often known as FX. This is a decentralized market and belongs to the over-the-counter section (OTC). This kind of trading is considered one of the most effective investment businesses for generating lucrative wholesome returns in a short span of time. However, due to lack of information if this trading is not carried out in a certain way it might lead to an offence in certain countries especially India. The Foreign Exchange Management Act, 1999[1] (FEMA) governs the legislation related to foreign exchange in India. India is one of the largest exporters who had to ease its financial market regulations bypassing certain rules and regulations through SEBI and RBI. This article covers all the important aspects and status related to Foreign Exchange trading and its legality along with its trade provisions.

Keywords: *legality, forex, trading, offence, provisions.*

INTRODUCTION

Forex, or foreign exchange, could well be defined as a group of buyers and sellers who exchange money at a set price. It is the process through which individuals, corporations, and national banks convert one currency into another - if you have ever traveled abroad, you have

[1] Foreign Exchange Management Act 1999

most likely made an FX exchange. While a lot of foreign exchange is done for practical reasons, most of the money exchange is done for the goal of profit. The amount of money moved on a regular basis can make the value of certain monetary types incredibly uncertain. This unpredictability very often draws the attention of retail investors: it offers an increased probability of handsome profits while also increasing the risk. It is one of the world's most important and liquid financial markets. With a daily trading volume of over 5 trillion dollars, this market is well-known around the world.

TYPES OF MARKETS

The forex market can be classified broadly on the basis of the below-mentioned types[2]:

- Spot market: a physical exchange of a currency pair that occurs at a time when the trade is being settled – i.e., 'on the spot' – or within a short period of time.
- Forward forex market: a commitment to purchase or to vend a defined quantity of legal tender at a given price, to be settled at a future date or within a range of future dates, is called a forward forex market.
- Future FX market: a contract to buy or vend a specific quantity of a specified legal tender at a specific price and date in the future is formed. A futures contract, unlike a forwards deal, is legally binding[3]

IS FOREX TRADING LEGAL IN INDIA?

When the Foreign Exchange Management Act (FEMA)[4] was implemented in India, things changed dramatically. The Reserve Bank of India (RBI) besides the Securities and Exchange Board of India (SEBI) became the watchdogs of Indian forex trading. The rules and regulations were in order, and they are still being revised to reflect the country's current difficulties. On a global trip to Europe, for example, if you converted your rupees (INC) into euros, the forex

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[2] *Ibid*

[3] Amandeep Sonewane, 'Can Indians trade forex legally' (*A to Z Market*, 27 July 2021) <https://atozmarkets.com/news/forex-trading-illegal-india/> accessed 16 October 2021

[4] *Ibid*

swapping scale between the two budgetary standards, based on the organic market at the time, determines the number of euros you receive in exchange for your rupees.[5]

This is the most dynamic and fluid market on the planet. It fluctuates minute by minute and day by day as currency prices fluctuate. London, Toronto, Paris, Amsterdam, Frankfurt, Milan, New York, Bahrain, Tokyo, Hong Kong, and Singapore have substantial business communities in the unknown trade. In India, RBI or the Reserve Bank of India, which is the country's predominant bank, monitors market trends and is committed to intervening as necessary, in accordance with public authority agreements.[6] The FEMA and RBI directives provide clear guidance on what is permissible and prohibited in terms of forex trading in India. To understand more about the legality of forex trading we have to look at the objectives of FEMA which are as follows-

- Facilitating international trade and payments
- Promoting India's foreign exchange market's orderly development and upkeep
- Establishing protocols and processes for all foreign exchange transactions in India.

WHAT DOES FEMA SAY ABOUT FOREIGN EXCHANGE?

Section 3 of FEMA,[7] states that as otherwise mentioned in this Act, rules or regulations made thereunder, or with the prevalent, exceptional permission of the Reserve Bank, no person shall-

(a)[8] trade-in or transmit any foreign exchange or foreign security to anyone who isn't a legitimate/authorised person;

(b)[9] make any remittance to or for the credit of anyone who lives abroad in any way;

[5] 'Is Forex Trading legal or not in India' (*Helpline Law*, 11 February 2021) <http://www.helplinelaw.com/national-and-social/FTLI/is-forex-trading-legal-or-not-in-india.html> accessed on 16 October 2021
[6] *Ibid*
[7] Foreign Exchange Management Act 1999, s 3
[8] Foreign Exchange Management Act 1999, s 3(a)

(c)[10] receive any remittance by order or on behalf of anyone who lives outside India in any way through a legitimate person. – An explanation. Any person in, or resident in, India who acquires any sum of money either by order or on behalf of any person residing outside India through any other person (including an authorised person) without a corresponding inward remittance from any place outside India is deemed to have received such payment for the purposes of this clause.

(d)[11] 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. —Just to bring out an explanation for the above-mentioned phrase, "financial transaction" literally implies the fact that making any payment to, or for the acknowledgment of any third person, or receiving any payment by either by command or on behalf of any other person, drawing, issuing or negotiating any promissory note or bill of exchange, or relaying any security or acknowledging any debt.

Section 4 states as otherwise provided in this Act, no person residing in India shall acquire, own, possess, hold, or relay any foreign exchange, foreign security, or any unbudgeable belongings located outside India. —Save as otherwise provided in this Act, no person residing in India shall acquire, own, hold, possess, or relay any foreign exchange, foreign security or any unbudgeable belongings located outside India."[12]

We can deduct from the preceding sections that trading in foreign currency is not entirely unlawful, but it is subject to some restrictions. The FEMA law allows Indian people to engage in forex, foreign securities, and own immovable property in other countries. This was permitted when either someone was in possession of the contract, security, or property while living outside of the Indian periphery or even when it was passed down to him/her by someone living abroad. Individuals and businesses moving money to and from the Indian subcontinent, as well as interchanging foreign currency in India for travel purposes, were

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[9] Foreign Exchange Management Act 1999, s 3(b)
[10] Foreign Exchange Management Act 1999, s 3(c)
[11] Foreign Exchange Management Act 1999, s 3(d)
[12] Foreign Exchange Management Act 1999, s 4

covered by FEMA compliance. Many other directives and modulations were enacted under the Act, covering specific concerns like document verification, adjudication, current account transactions, and appeal, compounding proceedings, permissible capital account activities, and borrowing or lending in currency, among others. According to the FEMA guidelines, there has been quite a number of limitations, such as if a person breaches a quota, the penalised amount would be thrice of the original. In events where the sum is not calculable, the penalty inflicted remains up to Rs. 2 lakhs. In cases where the periodicity of infraction is regular, the fine is Rs. 5000 per day which does not take into consideration the very first day of the breach. In addition, if any form of property is engaged throughout the training, the tender will be taken and treated as a charge, which is illegal.

Indeed, FEMA was created in order to liberalise India's foreign exchange market. The Act promoted foreign exchange deregulation and smooth international trade. FEMA also differs administratively from FERA, which intended to put broad controls on every facet of India's foreign exchange transactions. FEMA, contrarily, attempted to superintend only those forex transactions that could have a negative influence on national security and the economy as a whole and opened individual forex transactions to the free market. EURINR, GBPINR, JPYINR, and USDINR were previously traded instruments.[13] In any event, the Reserve Bank of India allowed traders to offer cross-money potential agreements and trade exchanged cash options with three more money pairs, namely EUR-USD, GBP-USD, and USD-JPY, starting on December 10, 2015. In India, only spot trading is prohibited, not futures or derivatives trading. It is permitted in India to trade in INR-based currencies with local brokers. To trade FOREX in India, you must first open a trading account with a local broker who is fully regulated by the government. After 2015, the restrictions became harsher. The RBI became extremely active and started making rules and regulations regarding such exchanges.[14]

PENALTY

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[13] *Ibid*

[14] *Ibid*

If any individual is found to breach any provisioned segment of this Act, or any rule, regulation, legislation, codification, or order issued in the exercise of powers under this Act, or any condition subject to which a Reserve Bank authorization is issued, he shall, upon pronouncement, be liable to a penalty of up to thrice the amount involved in the contravention, or up to two lakh rupees if the amount is not calculable.

WHAT DOES RBI SAY ABOUT FOREX?

The Reserve Bank had seen adverts from electronic/internet portals guaranteeing guaranteed large profits on foreign exchange trading or investing. Many companies even use agents who directly contact consumers to persuade them to participate in forex trading/investment schemes by promising disproportionate/exorbitant returns. RBI warns the masses not to send or deposit money for such illegal activities. Many residents have recently fallen prey to such appealing promises and lost a significant amount of money, necessitating the counsel.[15]

FOREX TRADING AND CORPORATIONS

Companies are permitted to execute their trades, but the condition for partnerships is that they can only use free cash from their stores. The companies, however, are not empowered to transfigure the native currency into dollars and then exchange it. They've also been tweaked to work with leverage of fewer than ten times.[16]

FOREX TRADING AND INDIVIDUAL TRADERS- REPORTS OF RBI

The individual dealers in India have additionally been cautioned by the RBI against the web-based exchanging entryways which offer these charming results of high gains however don't uncover to the merchants that they are catching themselves in a criminal behaviour considered by their state. RBI additionally distributed a notice that announced specific specialists who reached the merchants and encouraged them to put resources into forex to procure immense benefits. In this review, a considerable lot of people were caught in this unlawful managing of

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[15] RBI Advisory on Overseas Forex Trading through Electronic / Internet Trading Portals (Press Release: 2010-2011/1196)
[16] *Ibid*

foreign reserves. In addition, the majority of the exchanges done through these web gateways had an extremely negative influence.[17]

RBI ACTION AGAINST FRAUDULENT AGENTS

An additional report and survey by RBI revealed that people were asked to make marginal payments to their agents through debit cards or online portals and the same money was transferred to different accounts in different banks. This was a fraudulent activity against people who tried trading in foreign reserves. RBI has absolutely made it clear that if any person involved in such activities is caught, strict penalisations are bound to be inflicted upon him/her in accordance with the FEMA, 1999, contraventions. To stack onto it, he/she would also be held responsible for breaching the KYC norms and money laundering standards[18]. All the transactions that are proclaimed non-permissible under the FEMA act are also not allowed. These transactions comprises of exchanges related to foreign currency or marginal trading.

CONCLUSION

Through the medium of this text, it is clear that our regulations around foreign exchange and trading contain numerous loopholes. It is apparent that forex trading is not entirely prohibited in India. Certain types of dealing are forbidden and prohibited, and if they are practised, they will result in severe punishment and jail. As stated in Section 13 of the FEMA,[19] a person will be liable to a penalty up to thrice the sum which is involved in such contravention where the amount is quantifiable, or up to two lakhs where the amount is not quantifiable. Also, where the contravention keeps on continuing further penalty may extend up to five thousand rupees daily. Various brokers continue to attempt to defraud investors due to a lack of proper education among common investors.[20] The laws have been codified, and the Reserve Bank of India and the Securities and Exchange Board of India have taken steps to improve the laws, rules, and regulations. However, there are still a lot of modifications that need to be made.

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[17] *Ibid*
[18] Reserve Bank of India, A P (DIR Series) Circular No 46
[19] Foreign Exchange Management Act 1999, s 13
[20] *Ibid*