**Submissions to**
**His Excellency,**
**The Finance Minister**
**Government of India**

# Convertibility of Rupee and Exchange Rate

**BOMBAY CHARTERED ACCOUNTANTS' SOCIETY**
**Churchgate Mansion, 'A' Road, Churchgate, Mumbai 400 020.**

Date : 5th July, 1997

Honourable Finance Minister,
Finance Ministry,
Government of India,
North Block,
New Delhi,
INDIA

Your Excellency,

We are submitting herewith our views on Convertibility of Rupee and Exchange Rate of Rupee.

The Tarapore Committee report is an excellent report. A well defined plan of action is the right way of preparing and discussing national strategies.

Hopefully, our presentation will compliment the report and add a few concepts.

Some of the view presented by us are different from Government policies so far.

We submit that:

Most of the fundamentals in the Indian economy are good. We can make rupee fully convertible by 31st December, 1999 and remove all restrictions on imports and exports by 31st December, 2000.

FERA is doing more harm than good.

Modern, fast, competitive global markets do not permit a situation where businessmen have to take "prior permissions" for their legitimate business decisions. The delays cause loss of business and GDP.

Enforcement Directorate's human rights violations are unthinkable in modern democracy.

Hopefully, our views will be of some humble use to you.

We will be glad to personally meet, discuss and elaborate our views.

**For BOMBAY CHARTERED ACCOUNTANTS' SOCIETY**
**President**

**ASHOK DHERE**

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### SECTION I : CONSERVATIVE APPROACH



### SECTION II : RETHINKING THE FUTURE

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## ABBREVIATIONS

BOP : Balance of Payments.

BOT : Balance of Trade.

CAC : Capital Account Convertibility.

DFI : Direct Foreign Investment.

ECB : External Commercial Borrowings.

ECD : Exchange Control Department.

ED : Enforcement Directorate.

FX : Foreign Exchange.

GOI : Government of India.

RBI : Reserve Bank of India.

**PREFACE**

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| **Sound Economic Fundamentals Justify a Bold Approach. full potential may be Achieved when the Sentiment Improves.** | 1. WE PRESENT --<br>(i) Suggestions for action and a time table for the same;<br><br>(ii) A background, a perception of Indian economy based on which we have made the suggestions; and<br><br>(iii) Brief Logic for our suggestions.<br><br>1.1 Convertibility of rupee or replacement of FERA by FEMA can not be considered in isolation. Several economic and political factors have to be considered together.<br><br>1.2 At present, several economic fundamentals are good and can cause substantial industrial growth. Continuing liberalisation is not giving expected results as the "sentiment" is pessimistic. A crisis of confidence pervading at all levels does not allow the benefits to be gained to the full potential.<br><br>1.3 On convertibility of rupee and exchange rage, there are several reasons which can change over-cautious approach into optimism. |
| **Future will be Different Strategies will have to be different from the past**. | 2. **ROAD MAP**<br><br>2.1 You have used to words –<br><br>"ROAD MAP to convertibility"<br><br>The Words "Road Map" make one think of some of the most modern management gurus and we refer to the book "Rethinking the Future". Some ideas from the writing of Mr. Alwyn Toffler and Mr. Rowan Gibson are presented below:<br>(i) "People and institutions think that the future will be a projection of the past. It would be continuation of the same road.<br><br>Nothing is farther from the truth.<br><br>**The road stops here**. |

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| | For future, you have to make your own road and make new road maps.<br><br>(ii) If some ideas have succeeded in the past, the successful people and institutions become "prisoners of these ideas". This becomes the cause of their down fall because future will be different and the strategies that will work in future will different".<br><br>2.2 Compared to these modern thoughts,<br><br>Some theories followed in the past by Government and the RBI appear to need a fresh look.<br><br>Some such theories are:<br><br>(i) Devaluation of Rupee helps exporter; (para II 6.6.8 page 46);<br><br>(ii) Devaluations helps achieving BOT equilibrium; (para II page 43);<br><br>(iii) Inflation Differential must be reflected in exchange value of rupees; ( para II 6.2, 6.3 page 38 & 39 );<br><br>Each of these ideas is analysed in the paragraphs stated in the bracket.<br><br>2.3 India does not have plenty of time to achieve CAC.<br><br>(i) We have already lost a few decades -- during which nations poorer than India have now 3 times the Indian per capita GDP.<br><br>Growth is in progression. |
| **Global forces and trends do not leave much time and options for India**. | When one nation is ahead, it keeps going further much faster than the nation behind.<br><br>We need a quantum jump for recovering the time lost in the past.<br><br>Global forces & trends do not leave much time and options for India.<br><br>(ii) World Trade Organisation and others will not allow us to retain our import controls for long. We must |

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| | achieve global competitiveness - so that by 31st December, 2000; we can remove complete controls on imports. |
| | 3. Tarapore Committee Report is a landmark in liberalisation - Ad hoc approach is replaced by a well directed process; and a targeted time table. The fact that you have already started implementing recommendations is building confidence.<br><br>4. We understand that our report is not a complete submission. Financial institutional structure in the country, interest rate differences etc. are not covered by us. There are other policy issues that are not covered.<br><br>5. Our paper is presented at two levels:<br><br>(i) Our suggestions on convertibility of rupee as a continuation of the past. A Conservative approach.<br><br>(ii) Rethinking the future -- a fresh and radical approach at the issue.<br><br>6. This paper concentrates on convertibility of rupee, procedures under FERA and valuation of rupee (exchange rate). |

## SECTION : I
## CONSERVATIVE APPROACH

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**Nos.**



Paragraph (1) gives suggestions in brief.

Paragraph (2) gives explanations for the same in the same serial order.

## CONSERVATIVE APPROACH
## SUMMARY

**TIME TABLE**

### 1. BRIEF SUGGESTIONS.

### 1.1 NRI investments - Repatriability

Make ALL NRI holdings and investments in India fully convertible. This will include inheritances within India, earnings within India, NRO account, NRNR accounts and all investment and loans made under RBI permission on non-repatriation basis.

Announce the decision for this purpose **15th Aug., 1997**

Give actual effect to decision on a date not later than **31st Dec., 1997**

**NRI Investments - Procedures**

There are several investments that are being permitted to NRIs as on today - under various categories and notifications.

Make all these investments free from procedures. The NRIs may simply file form "DIM" - a declaration to RBI and go ahead and make their investments. **15th Augu., 1997**

### 1.2 Foreigners' Dues

As a step towards convertibility, Government / RBI should announce that all funds belonging to foreigners and foreign companies can be immediately remitted abroad. There are several cases of delay in their remittances.

Now that Indian has comfortable FX reserves, all their dues must be fully allowed to be remitted abroad. **15th Aug., 1998**

### 1.3 Read Tapism / Multiple Permissions

There should be single, final permissions. When FIPB gives permission, there should be no need to go to RBI.

When Central Office of the RBI gives a permission, there should be no need to go to regional office of RBI.

| | TIME TABLE |
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| RBI's policy of - "In Principle" and "Fianal" - two stage permissions should be abolished. The first permission itself should be "final" | **15th Aug., 1997** |
| 1.4 The Manner of RBI's liberalisations and permissions need improvement. Most liberalisations by RBI are with several conditions and provisos. Almost all permissions gives by RBI are accompanied by several conditions. | |
| All insignificant conditions should be removed. | |
| All liberalisations for shares should be applicable to debentures also. | |
| This simplification may be made effective immediately | **5th Aug., 1997** |
| 1.5 **Current Account Convertibility** | |
| India has announced convertibility of rupee on the current account. This is not fully implemented. There are bureaucratic hurdles and red tapism. There restrictions amount to violation of declarations made before the Parliament and IMF. | |
| Removal of all hurdles in current account convertibility will boost confidence in Government. | |
| Current account convertibility should be implemented fully and immediately. Any delay is further eroding confidence in RBI. | **15th Aug., 1997** |
| 1.6 Government notifications on liberalisations should be without unnecessary and insignificant conditions and provisos. | **15th Aug., 1997** |
| 1.7 Liberalising gold import and not allowing payment for the same is artificial. | |
| Allow free import of gold and free remittance of payments. This will considerably reduce the havala market. | **15th Aug., 1997** |

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| **As the 1st step towards convertibility, all NRIs should be permitted full remittance of their holdings in India**.<br><br>**Comfortable FX position permits risk taking**. | 2. **BRIEF EXPLANATIONS**<br><br>2.1 **NRI investment - Repatriability**.<br>Make all NRI investments in India fully repatriable.<br>2.1.1 We are not considering any ideology here. There is no comparison being made with residents' rights.<br><br>2.1.2 Foreign exchange market and investment market; like share market run largely on confidence and sentiment.<br><br>In the share market the promoter is most successful who gives genuine benefits to his investor. And a promoter who gives unexpected profits to the investors becomes everyone's darling.<br><br>By giving this gift of full repatriation rights to all NRIs, India will suddenly become a centre of attraction for all NRIs. Since this will be an unexpected bonanza; they would love to make even more investments in India.<br><br>It is true that some NRIs will take their investments out of India. We cannot estimate how much money will go out. However it is a reasonable estimate that the new funds inflow will be far more than the funds outflows.<br><br>This is, at best, an estimate. No one knows whether – on making non-repatriable investments as repatriable investments - the NRIs will take out more funds or bring in more funds.<br><br>It will be calculated risk.<br><br>However, present is the best time to take such risk.<br><br>As per newspaper reports dated 18th June, 1997; there are substantia FX inflows, reserves are swelling & government is worried over utilisation of increasing FX reserves ($ 28 billions). Government wants to utilise these reserves for import of capital goods and technology.<br><br>Using a part of the increasing reserves for NRI remittances will amount to building up more confidence in India; and taking a clear step towards CAC. |

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| | In any case, when rupee is made fully convertible in or around the year 2000; these remittances will be allowed. And convertibility will be in steps. Let this be the first step. Give NRIs an advance benefit and earn their confidence.<br><br>2.1.3 India may appear to have political instability. However, there are countries which have far more instability.<br><br>To our knowledge, some of the NRIs' sentiment is on the following lines: |
| **NRIs want a stable country for investments.** | Indian politics is more stable than the whole of Africa and Latin America. NRIs living in the Middle East do not keep their savings in the Middle East. Indonesia is a dictatorship<br><br>- NRIs living there do not plan to retire there. All these NRIs are constantly in search of a good, stable country for investment. They know that what happened to Kuwait can happen to several other city countries. These smaller countries may not exist in the global political map after a few decades. But India will be there as a country even after several decades.<br><br>So far, the rich NRIs have considered U.S.A. and U.K. as primary investment targets. There are several reasons. One chief reason is : they have suffered substantial losses by investing in India.<br><br>Despite these losses, NRIs have still made and continue to make investments in India.<br><br>GO ALL OUT to attract these investments on a large scale, Making existing investments fully repatriable is one such move. Other moves discussed are:<br><br>Appreciation of Rupee - Paragraphs II 10, page 64<br><br>Simplifying all procedures - Paragraphs I 2.3, 2.4 - pages 13 & 14 |
| **All foreigners should be allowed full remittance of their** | 2.2 **Foreigners' Dues**<br><br>There are different cases where amounts payable to |

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| **dues.** | foreigners are not allowed to be remitted. A few illustrations are given.<br><br>2.2.1 Foreign citizens, who worked in India might have saved certain amounts in India. At the time of retirement & return abroad, they are permitted to remit Rs.10 lakhs in the first year and Rs.5 lakhs per year thereafter.<br><br>2.2.2 Foreign companies might have shareholdings in the companies with which they have collaborated. For some reasons they may sell the shares and may want to remit the sale proceeds abroad - after payment of tax. Full amounts are not allowed immediate remittance.<br><br>When a decision is taken for full convertibility, we will have to progress towards it in steps. Permitting foreigners to take back their dues should be a right step in that direction.<br><br>We may first implement the repatriability for NRIs - say on 31st December, 1997. Then watch the implications for a few months. Foreigners may be allowed full remittance with effect from 15th August, 1998. |
| **Multiple Permissions" for the same transaction should be abolished.** | 2.3 **Red Tapism/Multiple Permissions**<br><br>2.3.1 One simple method of cutting down the bureaucratic delay: **Multitude of authorities**.<br><br>Today even when FIPB clears a DFI proposal, the parties still have to obtain a further permission from RBI. And even in such cases, there are several instances where RBI takes several months in granting final permission.<br><br>There are instances where Central Office of RBI gives a permission and then a further permission is required from regional office.<br><br>Such duplications must be absolished with immediate effect. Once FIPB grants a permission, there should be no need at all for obtaining any permission from RBI . If at all statistical information is required, a simple filing of declaration after completing the transaction may be provided for.<br><br>Similarly, where Central Office of the RBI grants a |

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| | permission, there should be no need for the applicant to go to any regional office - except for filing a declaration.<br><br>2.3.2 A characteristic red tapism is the RBI procedure where -- RBI first grants an approval "in principle". This approval is attached with several conditions.<br><br>Once the applicant fulfils all these conditions - like filing bank certificate for inward remittances etc. - a "final" permission is given.<br><br>**Consider an illustration**<br><br>RBI gives permission "in principle" to an OCB to invest in India say Rs. 50 lakhs. The shares and securities cannot be issued before "final permission" is given. Final permission will be given only after the OCB sends in the remittance, obtains a bank certificate for having paid the money into the Indian company and fulfilling several other conditions. This may take two or three months.<br><br>Till such time, the Indian shareholders with their paltry investment of - say Rs. 10,000/- remain 100% shareholders of a company which has Rs. 50 lakhs in the bank account. |
| ***Delay caused by multiple permissions cause avoidable anxiety*** | There have been actual cases of disputes developing within these two months. It is a real possibility that has to be considered. And the OCB remains in suspense, with no powers at all under the company law and the funds in control of other shareholders.<br><br>This suspense and delay are caused only by an obcession to ensure that all formalities are completed before RBI gives the "final permission"<br><br>Such two step permission procedure should be abolished with immediate effect. First permission itself should be a "final" permission. Several irrelevant conditions should be abolished. Some key conditions may be fulfilled by the applicant and appropriate declarations may be filed within the prescribed time.<br><br>Both these simplifications can be introduced with immediate effect -- say 15th August, 1997. |

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| | 2.4 **Reserve Bank's Approach**<br><br>We would like to place on records to appreciation that RBI has remained one of the finest institutions in India. Most of the institutions having statutory authorities have not been able to remain free from corruption, nor have they been able to maintain professional standards. The fact that RBI has been able to do so in current India position -- is highly commendable.<br><br>However, we have some different ideas and strategies which we would like to submit here. These are the differences which any two persons in a democracy may have.<br><br>There are some human frailties also. These are universal.<br><br>**Reserve Bank's Style of Functioning**<br><br>Reserve Bank has a particular style of functioning and we give a few examples:<br><br>2.4.1 **Transparency**<br><br>World over people move towards transparency. Whatever is the policy, rules and regulations; it should be clearly written and published.<br><br>RBI, however, believes in secrecy and keeping policy matters to itself. |
| ***Total Transparency in all procedures under FERA/FEMA* should be ensured.** | (i) There is a **Blue Book** of instructions. RBI officers keep it under lock and key. Public is not allowed access to it. Why there should be such a secrecy? If our applications are going to be considered by a policy, we have the right to know what it is.<br><br>Initially, even the RBI's Exchange Control Manual was not available to the public. Thankfully, for the last few editions, it is available to the public. RBI must publish the Blue Book also and any other policy guidelines which RBI or GOI may be following to determine any applications. |

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| | (ii) **Agriculture**<br><br>Non-Residents are not permitted to do agricultural business in India. We are not discussing at this stage for or against this policy decision. However, which section of FERA, rules, regulation, notification or circular says that RBI or GOI will not permit an NRI to do agricultural business? It is not given in any statutory announcement.<br><br>How can you have an important policy decision which you keep under lock and key?<br><br>Is it Democracy of the 1990s? |
| ***Insignificant conditions in RBI permissions should be abolished.*** | 2.4.2 **Unnecessary and Insignificant Conditions/Red tape**<br><br>Any time a permission is given by RBI, it is attached with several insignificant conditions. Consider a few illustrations.<br><br>(i) **Share Transfer**<br><br>When RBI grants approval for transfer of shares for example by an NRI to a Resident, it provides for a condition that the cost of brokerage and share transfer fees must be borne by the NRI.<br><br>Why should RBI provide for such conditions?<br><br>Why can't the parties to a contract decide who should make such payments?<br><br>In practice it is an insignificant amount and any one may pay it. However transactions worth crores of rupees have been held up because the RBI officer insists on a bank's certificate that the cost of brokerage and stamp fee was borne by the NRI.<br><br>Why should such irritants be permitted -- which, for totally insignificant matters cause red tape?<br><br>(ii) A.D (M.A. Series) Circular No. 20 dated October 28, 1996. |

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| | Disinvestment of shares.<br><br>In case, shares have to be transferred by private arrangement -- following conditions will apply:<br><br>(a) Shares can be sold at a price arrived at by taking an average of quotations for one week preceding the date of application. The daily quotation should be average of daily high & low. A variation of 5% on either side can be considered.<br><br>(b) In case of share transfer with passing management control, a price which is higher by up to a ceiling of 25% This, however, will be subject to conditions.<br><br>What is the sanctity of the share price of any week? Promoters have manipulated the price any which way they wanted. Investigations are going into such matters for years together and nothing happens. |
| ***All liberalizations for shares should also be applicable to debentures*** | More important issue is, why should RBI decide the price? Why can't it be left entirely to the parties who are transacting the business? How long can we go on with the suspicion that if allowed, people will do wrong?<br><br>Those who want to do wrong have gone ahead & did it. No authority has been able to prevent it. But genuine businessmen who want to transact business with appropriate - permissions get entangled into a cob-web of conditionalities<br><br>It does not mean that there should be no regulatory mechanism. In fact we are saying that the regulatory mechanism should be strengthened further so that the culprits are caught quickly and victims compensated. But regulators have no business interfering with genuine businessmen and their business transactions.<br><br>Paragraph 3 of the same circular gives detailed guideline on thinly traded shares.<br><br>All these are permissions / liberalisations for shares.<br><br>Why not cover debentures whether fully convertible, partly convertible or non-convertible?<br><br>In our submission, RBI or GOI should have absolutely |

no say as far as price are concerned. A liberalisation for shares must be applicable for all shares and securities.

2.4.3 **Being "above the Law"**

Compare the administration of Income-tax Act with the administration of FERA.

The Income-tax department has a clear hierarchy.

Income-tax Act cannot travel beyond the Constitution.

Income-tax Rules cannot travel beyond the Act

***RBI should not interfere in business decisions.***

CBDT circulars cannot travel beyond the Act and the Rules.

And all officers of the Income - tax department - from CBDT chairman to the assessing officer cannot travel beyond the Act, Rules, Circulars and notifications.

Consider following example under FERA:

**NRI loans**

Notification No. FERA 175/97-RB dated 27th Feb., 1997. Signed by Executive Director, RBI.

This notification permits an Indian resident to receive loans from NRI relatives provided that loan is interest free and non-repatriable. The notification does not provide for any conditions as to the use of funds.

***RBI circulars can not travel beyond the law.***

Based on the above notification, RBI has issued circular -- A.D.(M.A.Series) Circular No.12 dated March 12, 1997.

The circular provides that the loans taken cannot be used for, inter alia, purchase of immovable property, shares, debentures or for relending!

We have two objections --

Why should RBI interfere in the citizen' business decisions -- as to the use of funds? Why should it lay down several restrictions? In the guise of effective monetary controls can we as the nation allow such

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| | powers to RBI?<br><br>Secondly, how can the circular travel beyond the notification? When the notification does not provide for end-use restrictions, can the circular provide such restrictions?<br><br>Can the Chief General Manager, Exchange Control Department - travel beyond what is provided by the Executive Director?<br><br>2.5 **Current Account Convertibility**<br><br>2.5.1 You have announced that rupee is now **convertible on current account**. This means that all revenue expenses can be freely remitted outside. Incomes by Non-residents can be freely remitted outside. This is a declaration made by India to the International Monetary Fund (IME).<br><br>2.5.2 Article VIII of the IMF's "Articles" is produced below:<br>**IMF**<br>**Article VIII**<br><br>**General Obligations of Members**<br><br>"**Section 1**. Introduction<br><br>In addition to the obligations assumed under other articles of this Agreement, each member undertakes the obligation set out in this Article."<br><br>"**Section 2.** Avoidance of restrictions on current payments<br><br>(a) Subject to the provisions of Article VII, Section 3(b) and Article XIV, Section 2, no member shall, without the approval of the Fund, impose restrictions on the making of payments and transfers for current international transactions."<br><br>Does this article permit any artificial restrictions on the remittance of revenue expenses?<br><br>2.5.3 RBI circular - A.D.(M.A. Series) Circular No. 3 dated 16th January, 1997 gives a clear impression that |
| ***RBI can monitor but cannot sit in judgement over current account transactions.*** | |

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| | there are no restrictions on revenue expenses --<br><br>"India has accepted the obligations under Artcle VIII of the Articles of Agreement of IMF and accordingly, all bona fide current account transactions would qualify for release of exchange either under the authority delegated to authorised dealers or after obtaining the necessary approval from Reserve Bank."<br><br>2.5.4 Consider following instances-<br><br>(i) There are foreign shipping companies whose containers have been used in import of goods. The lease charges for the containers are not being allowed to be remitted abroad.<br><br>(ii) One company, relying on the fact that rupee is now convertible on current account, appointed a foreign company for a job. When the payment had to be made, bank referred the matter to RBI. RBI is asking "this job could have been done by an Indian company. Why did you entrust it to a foreign company?" And then RBI sent the company on a long round of obtaining permissions from Government authorities. |
| ***3 year after its announcement, the current account convertibility is still not complete.*** | 2.5.5 Having made all declarations, when RBI does not permit remittance of current account transactions -<br><br>It amounts to violation of the declaration made by India to IMF; by the Finance Minister to Parliament. It amounts to dishonouring RBI's notification by RBI itself.<br><br>This shakes confidence in India and Indian institutions.<br><br>2.5.6 Why should RBI come down from its macro level policy decision making and go into individual business decisions of Indian businessmen?<br><br>2.5.7 RBI has a suspicion that in the name of current account payment, people may make capital transfers abroad. This fear psychology may be answered in the following manners:<br><br>(i) In any case, Government is determined to make rupee fully convertible. While we are liberalising; the fear psychology has to give way to a liberal approach. |

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| | (ii) In the fear that someone will do wrong, you cannot deny genuine payments.<br><br>(iii) Please also refer to paragraph II.2, page 28.<br><br>RBI should be independent of the Finance Ministry also.<br><br>However, this independence should be at the macro level in monetary policy matters. Can the RBI claim to be "above the law" in individual applications? Even Bundes Bank does not claim to be "above the law".<br><br>2.6 **Government Notifications**<br><br>The love for imposing unnecessary conditions is infectious. Consider a notification issued by Government and the conditions imposed :<br><br>Notification No. F10/22/90-NRI cell dated 17th July, 1992 as amended upto 5th January, 1994.<br><br>This notification permits an Indian resident to hold -<br><br>(i) Foreign Exchange in the form of coins;<br><br>(ii) Foreign currency upto $ 500 for "NUMISMATIC" purposes;<br><br>(iii) Foreign currency upto $ 500 for "PERSONAL" purposes.<br><br>A limit of $ 1,000 plus coins is understandable.<br><br>However, why the restrictions about the purpose for which it is kept?<br><br>How does one prove that he has kept the currencies for "numismatic" purposes ? If the notes are in an album, it may be okay. But if they are in a purse it may not be okay! What purpose is served by imposing such restriction?<br><br>And what purpose is served by imposing a restriction that $ 500 can be held for "personal" purposes? Imagine a situation where a businessman, a minister or a bureaucrat goes abroad for his official business. He returns to India with a surplus of a $ 10 currency note in |
| ***Unnecessary stipulations in GOI notifications may be removed.*** | |

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| | his pocket. He knows that in a few months, he has to go abroad for another business tour. So he retains the currency note $ 10.<br><br>This would be a violation of S. 14 of FERA.<br><br>The man has neither kept the amount for "numismatic" purposes; nor for "personal" purposes. He has kept it for "business" purposes.<br><br>The businessman or minister or bureaucrat can be arrested for this reason. He can be taken to the enforcement office, detained overnight and third degree methods can be used to get a confessional statement.<br><br>For all such human rights violations, the Finance Ministry would be directly and morally responsible.<br><br>We recommend a simple permission that "any Indian resident can hold foreign exchange worth upto U.S. $ 1,000".<br><br>2.7 **Principles of drafting Laws**<br><br>We refer to your lecture at Mumbai on 13th June, 1997 on the subject of "New Companies Bill". Following table, first column is extract of your talk as reported in Times of India, Mumbai, 14th June. Second column gives our comparison with FEMA. |
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| | Sr. No. | Your comments on Companies Bill | Our suggestions on FEMA |
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| *All the principles enunciated by you for new Company* | 1. | Government will have no discretion in company affairs. | Government & RBI should have no discretion in individual matters. Their authority should be only at macro policy level matters. |

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| ***Law should also be carried to FEMA.*** | | | |
| | 2. | Bureaucratic meddling has managed to spike many ideas. | Government and RBI have spiked innumerable investment ideas and damaged economy. -- under FERA. |
| | 3. | Dangers of giving Government discretionary powers are clear. | Because of enforcement directorate, giving discretionary powers is criminal.<br><br>Because foreign investment and foreign exchange are very important for the economy, it is even more important (than company law) that Government, RBI and ED should have no discretionary powers and ED should be wound up. |
| | 4. | Company law shall be "market driven" rather than- "bureaucracy driven" | It is important that the Foreign exchange flows - both in and out of the country should be market driven.<br><br>A consistent attempt to force the flows has resulted in the massive outward flight of the capital. |
| | 5. | We got professionals and judges to draft company law | Do the same for FEMA & Anti-Money Laundering (AML) laws. |
| | 6. | Company law should be potent instrument in fuelling growth and development. | FEMA should be such an instrument. |
| | | | AML should keep away mafia & drug traffickers. |

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| | **Summary**<br><br>Businessman should be left to himself. Normally, he is supposed to work honestly. Regulatory system should strike when a businessman is found doing something wrong. At such times, the punishment and compensation should be quick, decisive and exemplary.<br><br>Your approach stated in the above referred talk by you may please be carried to FEMA and Anti - Money Laundering laws.<br><br>The policy of "prior permissions" and bureaucrats sitting in judgement over business decisions is a "colonical" approach and must be abolished at the earliest.<br><br>2.8 **Gold Import**<br><br>2.8.1 A prohibition to import gold was a gift of a billion dollar business by the Government to the smugglers and the havala racketeers. |
| ***Artificial restrictions on import of gold and payments for imported gold should be done away with.*** | When gold import was liberalised, initially, the smugglers were worried. Soon they realised that they do not have to worry. Government has still left good business for the smugglers and havala racketeers. Government imposed two conditions that –<br><br>(i) Only an NRI who had been out of India for at least six months could import five Kilogrammes of gold; and<br><br>(ii) No payment (outward remittance) will be permitted for gold import.<br><br>In paragraph II 3.2, page 30 - we have discussed how Government regulations create a market for the smugglers and then a complimentary market for the havela racketeer for payment for smuggled goods.<br><br>2.8.2 It is a practical fact of life that primarily, a normal |

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| | NRI has no interest in bringing mint gold and keeping it in India. Some NRIs may bring small amounts as a favour to friends & relatives. But no one gives gold to any one free of charge. He would want the price of gold and would want to take the price back to the country of his residence. This is not permitted by law.<br><br>Under the present scheme, a regular gold jeweller who wants to sell jewellery in India cannot import gold. Normal NRIs also would not want to bring in the gold. So honest businessmen are out.<br><br>2.8.3 Smuggler is in<br>Instead of sending the gold through the porous border of India, he can now send it officially through the customs. He has to only catch hold of the cooks and drivers in the Middle East, give them a free return ticket and send the gold through these carriers. Customs cannot prevent the carriers. The smuggler has to arrange to collect the gold at the Indian airport. The carrier goes home, meets his relatives and goes back to the Middle East for his job.<br><br>2.8.4 The havala racketeer also has not lost his business. In fact, his business has increased. Now more gold comes in India and outward payment is not allowed. Government probably believes that since outward payment is not allowed through the banking channel, it doesn't have to face the impact on BOP.<br><br>2.8.5 This is wishful thinking.<br><br>Full payment for all imported gold has to go out. Only, it goes out through the havala market.<br>It has its own impact on the BOP. The NRI remittances which would have come in through the banking channel do not come in. It gets set off against the smugglers' gold import transactions. |
| ***Similarly, silver, and diamond imports and exports should be freely allowed.*** | This has even more impact that the impact of normal payments for imported gold. A payment by havala system carries a premium ranging between 10% and 15%.<br><br>2.8.6 We recommend that --<br>(1) Import of gold (mint) should be freely allowed to |

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| | anyone who wants to import. Very soon accredited businessmen and institutions will star importing and trading gold.<br><br>(2) All licensing and other procedures for import of gold, silver and diamonds should be scrapped. A jewellery exporter should have absolutely no need for any permission and no fear of any inspector knocking his doors.<br><br>This may help the Belgium based diamond merchants to set up shop in India rather than Belgium.<br><br>(3) Free, official payments should be allowed to anyone who is importing these items.<br><br>This will be a concrete step towards real convertibility on current account. And it will also wipe out the havala markets.<br><br>While the havala market is going on, no one can have a fair idea of the implications of any liberalisation or other measure on the Balance of payments. |
| ***Havala Market obliterates a clear vision of the impacts of liberalisation.*** | Measures discussed so far, which can increase outward flow of FX may be introduced in steps-<br><br>Free Gold import and remittances — 15th Aug., 1997<br><br>Full Current Account convertibility — 15th Aug., 1997<br><br>All NRI dues - fully repatriable — 31st Dec., 1997<br><br>All Foreigners and foreign Companies dues to be allowed immediate remittance — 15th Aug., 1998 |

## SECTION : II

## RETHINKING THE FUTURE

### A RADICAL APPROACH

| | RADICAL APPROACH<br>ASIAN FINANCE AND TRADING CENTRES IN INDIA |
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| ***The target in drafting FEMA should be to encourage growth of Asian finance and trading centres in India.*** | 1.1 **Finance Centres**<br><br>1.1.1 Mumbai can be an Asian Finance Centre with established associations allover the world. Madras and Bangalore can develop as finance centres attracting NRIs from the Middle - East and the South - East. Calcutta may specialize on China, Nepal and Bhutan. Delhi can be a Finance Centre establishing relations with Russia and Europe.<br><br>1.1.2 While drafting FEMA and anti - Money Laundering laws, it should be considered that the laws do not come in the way of natural development of India as an international finance centre.<br><br>1.1.3 The specialisations stated above should not be directed by law. They may come about naturally.<br><br>1.1.4 The moment, draftsman start developing the law with this idea in mind, entire concept of controlling the Indian residents will be replaced by a Globalisation concept.<br><br>1.1.5 As an important step towards establishing international exchanges in India, trading in all GDRs and ADRs of Indian companies should be permitted on Indian stock exchanges. For introduction of trading in FX denominated securities, necessary institutional infrastructure should be created - SEBI competent to deal with it. By a law it should be provided that no state Government or other authorities can levy and tax or stamp duty on these transactions. Custodial companies should be established. This will be a complete package of issues by itself.<br><br>1.2 **Trading Centre**<br><br>1.2.1 Hong Kong developed as an international trading centre based on China.<br><br>Dubai developed as an international trading centre because, inter alia, India and Pakistan controlled and regulated international trading. Left India do its own international trading. |

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| *WTO will force us to open up trade earlier than we would like.* | 1.2.2 Whether we like it or not, with World Trade Organisation, we have no options. We will have to open up our economy for imports from everywhere. India is trying to postpone these pressures and asking for nine or seven years time.<br><br>Why?<br><br>1.1.3 Because India is convinced that India cannot withstand global competition.<br><br>As long as RBI and Controller of Imports and Exports will regulate & control business, India will remain unable to compete globally.<br><br>1.1.4 Imagine 25 cities in Inida developing like Hongkong, Dubai and Singapore. This will be possible only when S. 18 of FERA is scrapped and the entire Import policy is scrapped (except drugs and weapons trafficking). Stop forcing every exporter of goods and services for bringing in their FX earnings into India. When the entire control atmosphere will go, the exporter will be truly left free to do his business.<br><br>Ultimate aim should be that theses cities should be Global finance and trading centres. |
| **Rupee IS fully convertible for those who do not care for the law.** | **2. PRESENT STATUS OF RUPEE CONVERTIBILITY**<br><br>Several authorities are taking exchange regulation very seriously. RBI considers investments abroad permissions ceremoniously with all the seriousness. If any one is caught with a violation of FERA, the poor man is half dead even before the ED pronounces final punishment. This seriousness of exchange regulation is only for those who want to abide by the law.<br><br>Those who want to circumvent or violate the law, rupee is already fully convertible.<br><br>Let us see some example.<br><br>2.1 RBI and Commerce Ministry used to take inordinately long time in permitting joint ventures abroad. And they would simply refuse permissions to partnership firms and |

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| | individuals.<br><br>Diamond merchants found out the simplest method of sending one family member abroad and making him nonresident. No permission would be required from any Indian authorities. This is one industry which is most successful in the field of setting up business abroad. Most of the industries / group closely supervised by RBI / ministry are not successful.<br><br>2.2 Businessmen, politicians and bureaucrats who wanted to transfer capital in or out of India have always treated rupee as convertible. They have transferred money at their will and more efficiently than the banking system.<br><br>2.3 Dr. Man Mohan Singh had estimated that Indian residents' black money in the Swiss banks is worth $ 50 billions.<br><br>This was in the year 1991.<br><br>Mr. Forbes (Jr.), Chairman, Forbes maganize had estimated, in the year 1996 that Indian residents' total wealth abroad may be near $ 150 billions.<br><br>No Indian authorities can make any dent in this situation - except by announcing "immunity schemes"! All the Government authorities are like the stable chowkidars running up and down after the horses have bolted. They take out all their rage on the timid and sick horses who could not run away and hence are still within India. |
| **Strictest of the laws are ineffective against smuggling and havala.** | 2.4 Under the Indian judicial system, it was very difficult to ensure that the ED could have won any cases against FERA violators. This was because, proving an offence and mala fide intention; taking exemplary penal action against smugglers was most difficult. So Government adopted some unique methods. It acquired massive powers under FERA which do not exist under any other laws in India. And Government brought in COFEPOSA & SAFEMA with even more powers.<br><br>With all these powers, the smuggling and havala transactions have gone on unabated. In reality, the real big smuggler, businessman or politician is never punished for diverse reasons. It is only the small businessman who is terrorised and the non-resident investor who is scared away. |

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| | Redundancy and harmfulness of FERA is established.<br><br>The reason for such a situation are discussed in the next paragraph.<br><br>3. **GOVERNMENT MONOPOLY OVER FOREIGN EXCHANGE**<br><br>3.1 **Legislative Package**<br><br>In the early fifties, Government decided to establish a total monopoly over all foreign exchange resources.<br><br>FERA provided that all FX earned by any Indian resident belonged to the Government of India and even an exchange earner cannot use it for his requirements. All dealing in FX including rate determination was the monopoly of GOI and RBI. |
| **A whole package of laws to establish Government monopoly over FX.** | Import licensing sought to ban import of goods considered luxuries and reduce the import of other items. Import licensing was supposed to regulate / reduce the demand for FX.<br><br>Customs duties made imported products costlier and provided revenue to the Government.<br><br>Both - import licensing and customs duties provided tremendous protection to the Indian industrialists and businessmen.<br><br>SAFEMA & COFEPOSA are supposed to deal with hardened smugglers.<br><br>A perfect combination of laws to establish Government monopoly over foreign exchange.<br><br>3.2 **Impact of FX legislation**<br><br>Import licensing created a wall, a barrier around India. Goods which were available outside India were not available within India. |

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| **The package really gave a dream market for the smuggler.** | Customs duties made imported products costlier.<br><br>Law abiding businessmen would not deal with goods not allowed to be imported.<br><br>All these together created a dream market for the smuggler. He had a ready market, almost no competition and a tremendous price difference between Dubai and Mumbai. The havala market for NRI remittances developed to compliment the smuggling by completing the cycle of payment for smuggled goods.<br><br>No legal system can even eliminate such a profitable business.<br><br>Government believed that by passing a set of laws, it can achieve its targets even if they are contrary to market forces. The smuggler used the same set of laws to increase his business and profits phenomenally.<br><br>The smuggler had a profitable business with no direct and indirect taxes and no investment in factories etc. He commanded such huge financial clout that he could establish influence with the politicians, customs officers, businessmen and film stars.<br><br>For any economist, this was a telling result of Government's attempt to contradict market forces. But Government and its institutions refused to see the writing on the wall.<br><br>So nature has caused a dramatic scene with double impact.<br><br>3.3 **The Jain Havala Case**<br><br>3.3.1 In the Jain havala case top politicians of almost all parties have been alleged to have resorted to havala or bribes. They may be innocent. But public feeling may be different.<br><br>The issue is, the market forces can be so strong that any one can get tempted. And a large majority of people are prepared to believe that almost anyone could be involved in violation of FERA.<br><br>The law has lost ALL respect from public minds. It is an unenforceable law which terrorises only the law abiding citizens. |

3.3.2 There is another implication of the Jain Havala Case. Consider market practices.

Normally, an Indian resident transfers money into or out of India through the havala agents. Once the transaction is completed, there will be no evidence left - except - the havala agent's diary. In most cases of such FERA violations, the ED's main reliance is havala agent's daiary or similar nothings in different forms.

Everyone knows that a third party's writing cannot amount to an evidence of any material value before a Court of Law. Hence the usual course adopted by the ED was / is to terrorise and browbeat the accused into signing a confession. The confessions are dictated by the ED officers and the accused signs on the dotted line. Armed with the havala agent's records and the accused person's confession, the ED could prosecute the people.

3.3.3 In the Jain Havala Case, ED could not force the accused into signing any confessions. And all cases fell flat.

However, there is an important development. The courts have now clearly held that the havala agent's records are no evidence. Even the persons accused to be havala agent have been acquitted.

**3rd party evidence is not good.**

3.3.4 Now all the lawyears and the public will be emboldened. Except for the persons caught in the act of transfer of money, no one may be successfully prosecuted.

**Jain Havala Case has further diluted ED's authority.**

Whatever little teeth that the enforcement directorate had, have been extracted by the Jain Havala Case.

FERA will have no powers to deter the powerful who want to violate FERA. But it will continue to be a source of terror for the ordinary people.

3.4 **Causes of outward flight of capital : Past :**

3.4.1 We had high tax regime.

Income-tax 97%

Wealth-tax 8%

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| **Excessive Taxes, Regulations and devaluations have caused outward flights of capital.** | Estate Duty 85%<br><br>These rates, in addition to artificial additions and disallowances.<br><br>No person (almost) who was in these tax brackets could remain honest.<br><br>3.4.2 Indirect taxes in the form of import duties, excise and sales tax were also very high.<br><br>3.4.3 Excessive economic regulation from all sides frustrated genuine entrepreneurs.<br><br>3.4.4 Rupee was continuously depreciating. Anyone who kept his wealth in India rupee, lost. On the other hand people who transferred their wealth abroad, benefited.<br><br>All these together were, inter alia, the causes of flight of capital outwards.<br><br>They also made India economy a high cost economy incompetent to compete in open, global markets. |
| **Today Indian economy favours a flight of capital inwards.** | 3.5 **Current Probabilities**<br><br>That nightmare is a past.<br><br>Today India has a direct tax rate regime which is most favourable to the businessman.<br><br>Indirect taxes are coming down.<br><br>Bureaucracy and red tapism has started – through extremely slowly - going down.<br><br>Today, Indian economy offers a rate of return higher than the rate offered by most of the countries. The foreigner is not prepared for bureaucracy and its damages. But the Indian businessman is accustomed to it. Indians know that if only they could bring back all their wealth kept abroad in tax havens, they could earn more in India. (- net of exchange loss and Indian taxes).<br><br>They are not bringing in full amounts because of the fear of FERA - FEMA and tax laws. |

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| | The VDS scheme as announced is not adequate (See paragraph 8, Page 51).<br><br>If FERA is totally scrapped and FEMA does not have sections comparable to S.9 and 16 of FERA, there can be an inward flight of capital. Slowly at first but a strong current in two to three years time.<br><br>4. **FX GAMBLING**<br><br>4.1 In the past, **FERA had three objectives:**<br><br>4.1.1 Conservation of precious foreign exchanges;<br><br>4.1.2 Regulating / preventing foreign business presence within India;<br><br>4.1.3 Stabilising conversion rate of Indian rupee.<br><br>4.2.1 Today GOI and RBI are more concerned with utilisation of surplus reserves rather than conservation of scarce FX.<br><br>4.2.2 And instead of preventing foreign investment, Government is going all out of its way to attract foreign investment. So the entire paradigm has to be shifted.<br><br>4.2.3 Only important issue is to maintain stability of Indian rupee.<br><br>4.3 Today, speculation in Indian rupee is restricted and gambling is just not allowed.<br><br>4.4 In the words of "Asian Wall Street Journal" FX dealing is really a "gamblers' den". Once a currency is fully convertible, there is very little control that a Central Bank can exercise over gamblers playing havoc with its currency. People like George Soros are on the look out for any currency which has a wide disparity between the prevalent market rate of the currency and<br>a value which in their perception is the sustainable value. When why find a currency, they go all out with their gambling to wipe out this difference.<br><br>If these gamblers decide to gamble on Indian rupee and if RBI ever tried to intervene, the current FX reserves of around $28 billions can be used up in a day. |

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| **Main objective of FEMA should be maintaining Rupee stability.** | 4.5 This danger has to be answered in two manners:<br><br>4.5.1 Rupee rate should be brought to a "sustainable" level. (This does not necessarily mean depreciation of rupee.)<br><br>FX markets must be made deeper and broader.<br><br>India's international trade and investment should increase considerably.<br><br>4.5.2 Unit this situation is achieved, RBI should be entrusted with powers that could prevent gambling in Indian rupee - whether by Indian gamblers or foreign gamblers.<br><br>4.6 The objectice and drafting of the legislation; and administration of the legislation should be towards protecting Indian rupee from FX gamblers.<br><br>4.7 RBI should be given a period of three years within which it must create a situation enabling full convertibility of rupee.<br><br>4.8 It may also be appreciated that the gamblers generally cannot decide a rate. The rates are determined by market forces. Gamblers only try to find out a currency where the rate supported by a Central Bank is different from the rate which market forces can sustain. If the difference is large, they strike and make a killing.<br><br>4.9 Can India consider appreciating rupee with full convertibility?<br><br>4.10 Market rate of rupee is Rs.36/- per dollar. PPP rate is Rs.9/- per dollar.<br><br>A rate which may achieve an "equilibrium" between exports and imports may be arrived at by annual adjustment of inflation difference between India and U.S.A. Assume for a moment that this rate may be Rs.40/-<br><br>4.11 **An Apprehension:**<br><br>If rupee is fully convertible and RBI tries to even maintain a rate of Rs.38/- ; then the FX gamblers can strike and force the rate to go down to Rs.40/-. |
| **Maintaining** | This may not be correct. |

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| **regular inward flows is touch Easy options have damaged economy.** | 4.12 In the market the rate is determined by total "Balance of Payments" and not just by "Balance of Trade".<br><br>If the total inward flows are larger than the total outward flows, then the rupee should go up. And FX gamblers cannot disturb such appreciating currency.<br><br>4.13 The issue is whether inward remittances can be sustained! If the inward remittances cannot be sustained; then very soon there may be a need to depreciate the rupee.<br><br>Such uncertainties cause difficulties for the economy.<br><br>4.14 Real answer to this question is to ensure an economic, tax and legislative environment where sustained inflows of capital are maintained. This is a tough task.<br><br>GOI and RBI have so far opted for the easier option of continuously depreciating rupee.<br><br>5. **DERIVATIVES & OPTIONS (D & O)**<br><br>5.1 In 1991-92 when share market started going through the roof, Government was happy and claimed it to be the result of liberalisation. When someone raised the issue that SEBI and other regulatory mechanisms were not capable of dealing with liberalised markets, the answers from the Government were - "let us liberalise first. We will take care of regulation a little later."<br><br>In 1992 when the securities scam was exposed, the whole Government was paralysed and economy went down.<br><br>5.2 When the scamsters were exposed fully, it was known to the public that several promising peoples' lives were ruined - by a few people.<br><br>The public response and the newspaper editorials and articles were blaming that the Government was at the fault.<br><br>The scamsters are free. If they address a seminar, the hall will be full. It they give interviews, leading financial papers publish them on front pages.<br><br>5.3 Securities scam was not the last. M.S. Shoes and other small & big scams keep coming out. Every time Government |

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| | is blamed. |
| | 5.4 In our view, the nation is swept over by a wave of greed. |
| | The small investor is greedy. He wants 50% returns in less than one year. |
| | The promoters are greedy. They want premiums based on project reports. |
| | Merchant Bankers and other intermediaries are greedy. For heir fees, they will support any scamster. |
| | No statutory authority can save the situation when everyone is greedy. The greedy people deserve what they get. |
| | 5.5 Despite this clear position, when CRB scam broke out, all the editorials and articles were screaming at the Government. Everyone wanted to decide which authority was at fault - RBI or SEBI or ROC! Mr. Bhansali, his brokers and the investors were a non-issue. |
| | You carry a heavy burden of public criticism. Which is some times unjustified also. |
| | 5.6 In this situation, you want to permit Derivatives and Options!!! |
| | Most potent instruments that the gamblers use. |
| **Indian Government carries a heavy burden of harsh, unjustified criticism.** | After Barings Bank's insolvency, its chairman (now retired) Lord Baring confessed that "I do not understand Derivatives and Options." |
| | **D & O have strong potential of bringing about crises.** |
| | How many persons within Indian regulatory authorities understand D & O? |
| | What market intelligence mechanisms do you have to catch the culprits? |
| | If without adequate preparations you open up these volatile instruments, are you not inviting fresh crises in the economy |
| | - Similar to the securities scam of 1992 & CRB scam of |

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| | 1997!<br><br>6. **DEVALUATION**<br><br>6.1 Government has consistently devalued the rupee. Probably following theories / stratgies are behind this policy.<br><br>6.1.1 Inflation differential between India and its major trading partner must be compensated by devaluation / depreciation of the rupee. (paragraphs 6.2 & 6.3)<br><br>6.1.2 Devaluation helps exporters. (Paragraph 6.4, 6.5 & 6.8)<br><br>6.1.3 Devaluation curbs imports and thus gives protection to indigenous industry.<br><br>6.1.4 Devaluation of Rupee creates equilibrium in Balance of Trade account. (Paragraph 6.5)<br><br>We believe that the Indian rupee is extremely under valued.<br><br>All the above stated theories are not applicable to Indian economy at the present time. |
| **Indian rupee is undervalued.** | Purchasing power parity and Demand and Supply are two important theories for determination of exchange rate. Let us consider both the methods one after the other. Let us consider Indian rupee and U.S.$. The principles will apply to several other currencies.<br><br>6.2 **Value of Rupee on Purchasing Power Parity (PPP)**<br><br>6.2.1 We can compare similar baskets of goods and compare their cost in Bombay (or Delhi or any other metropolitan city) and New York (or Washington etc.). An easy and comprehensive method of considering a basket of goods may be monthly cost of living for a family of four.<br><br>In New York, a family spending $ 2000 per month can live a lower middle class standard of living. A similar standard of living may be enjoyed by a family in Bombay for Rs. 4,000 per month.<br><br>This would give a conversion rate of Rs. 2 per U.S.$.<br><br>There are several forces other than consumer goods prices |

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| | which should go into determining the exchange rate. It is generally accepted amongst economists that in India, the difference between the PPP rate and the market rate is in the ratio of four. For a market rate of Rs. 36, the PPP rate should be Rs.9 per dollar.<br><br>6.2.2 World Bank, in its annual report for the year 1997 has given per capital, annual GNPs of various countries in terms of market rates and PPP rates. As far as India is concerned, the ratio of four between the two rates is roughly followed for several years.<br><br>We believe that based on PPP, the real value of the rupee should be Rs.9 per dollar.<br><br>6.2.3 We are aware of the strong objections which such a statement provokes and we shall deal with each one of them (So far as we are able to do so.) |
| **PPP value of rupee is Rs.9/$** | Before dealing with all these objections we submit two issues:<br><br>(a) We are not suggesting that the price should be brought back to Rs.9/- We suggest that rupee should be allowed to apprecate by 2% to 5% per year if the BOP pressures cause such an appreciation.<br><br>(b) We will highlight the losses due to devaluation of rupee.<br><br>Rupee value through demand and supply forces is discussed in paragraph 10.2 page 64.<br><br>6.3 **World Development Report 1997**<br><br>In this annual report, World Bank gives per capita annual GNP of several countries for the year 1997. Local currency GNP is converted into U.S. currency in two manners:<br><br>(i) At market rate; and<br><br>(ii) At Purchasing Power Parity.<br><br>6.3.1 World Development Report per capital GNP<br><br>Following countries have their local currencies' market values higher than the PPP rates. |

| Country Name | GNP at Market Rates | GNP at PPP Rates | Ratio |
|---|---|---|---|
| U.S.A | 26,980 | 26,980 | 1.00 |
| Sweden | 23,750 | 18,540 | 1.28 |
| Germany | 27,510 | 20,070 | 1.37 |
| France | 24,990 | 21,030 | 1.19 |
| Switzerland | 40,630 | 25,860 | 1.97 |
| Denmark | 29.890 | 21,230 | 1.41 |

Following countries have their local currency values at market rates lower than the PPP rates.

| Country Name | GNP at Market Rates | GNP at PPP Rates | Ratio |
|---|---|---|---|
| China | 620 | 2,920 | 0.21 |
| Brazil | 3,640 | 5,400 | 0.67 |
| India | 340 | 1,400 | 0.24 |
| Bangladesh | 240 | 1,380 | 0.17 |
| Indonesia | 980 | 3,800 | 0.26 |
| Malaysia | 3,890 | 9,020 | 0.43 |
| Thailand | 2,740 | 7,540 | 0.36 |
| Kuwait | 17,390 | 23,790 | 0.73 |
| Russia | 2,240 | 4,480 | 0.50 |

6.3.2 **Observations**

1. It is not just that poor countries have their currencies valued lower than the purchasing power. Even the rich countries of the Middle-East have their currencies valued

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| | low.<br><br>Common factor in all countries having low value of currencies is that they are suppliers of raw materials and other "low value addition" items.<br><br>Common factor in all countries having high value of currencies is that they have experts in economics. These people negotiate and manipulate world markets in such a manner that the terms of international trade are in their favour.<br><br>They benefit when they import low cost raw materials. They benefit when they export finished products - because they get higher values than added by them.<br><br>2. We believe that it is a manner of clever bargaining to make all suppliers lower their currencies. Encourage them to a competition in devaluing their currencies. Enjoy the fruits of low cost supplies. |
| **Wealthy nations force developing nations to lower the value of their currencies.** | This is the reason why (as per newspaper reports) a U.S. official had come to India in the year 1997 and urged the Indian Minister for agriculture to devalue Indian currency so that Indian foodgrains can be competitive in the world market. It was a great satisfaction to read in the paper that the honourable minister had refused to oblige.<br><br>When these western experts fail in persuading one country, they go and persuade some other country. If one major raw materials supplier devalues its currency, others have to follow.<br><br>This can be a reason why Pakistan has recently devalued its currency.<br><br>3. The Western World experts advise us as if it is in "OUR interest" what actually is against our interest and "IN their" interest. IMF, World Bank and other agencies are used as a tool in implementing their policies.<br><br>4. There is a co-relation between the following two statements -<br><br>"Some of the rich countries have their currencies valued high." |

"Because their currencies are rated high, they are rich."

5. These are the world trade practices. We cannot consider them sentimentally or politically. The most powerful countries write the rules of the game. And they write the rules in their own favour.

We have to play the game of international trade.

**Powerful countries write the rules of international trade in their favour.**

If we appreciate the purpose of their rules, we are better prepared for the game.

6. The issue is, rupee is already extremely undervalued. There is no need to depreciate the value of rupee and offset the inflation differential between India and U.S.A.

6.4 **Competitive Devaluations**

India's competitors in the world trade are other "commodity/low value products suppliers" like China, Bangladesh, Pakistan, Brazil etc.

When Indian Government devalues the rupee to help Indian exporters, all these countries also devalue their currencies. In this cycle of competitive devaluation; none of the raw material supplier country benefits.

The western, developed nations benefit in terms of getting their raw materials cheaper from all the countries.

**Offsetting inflation differential is out of question.**

We must not start the self damaging cycle of devaluations.

If, however, a major competitor starts the devaluation, we can not prevent the vicious cycle.

It is necessary that in all the trade and cultural blocs and outside the blocs, wherever India can influence opinions; it must convince the competitor to co-operate and to stop this cycle of competitive devaluations.

6.5 **Devaluation and Balance of Trade (BOT)**

It is believed that a devaluation of the currency helps achieving an equilibrium in the Trade Balance. It makes export more attractive & imports costlier. So exports increase & imports reduce. Thus an equilibrium is achieved.

**Competitive devaluations only**

**benefit the wealthy nations.**

Last forty years experience shows that we have never achieved a position where exports are equal to or more than imports. Wherever there is a massive devaluation, there is some short-term fall in imports, a jump in exports and we may see that for one year or so the trade deficit is very small.

However, our imports are largely inelastic. Through import licensing we have always avoided all the imports that could be avoided. And what cannot be avoided has to be imported at any price. Devaluation only causes a cost-push-inflation. Until the economy settles after a devaluation shock, there may be a short period drop in imports. A sustained reduction in imports can only be achieved by import substitution and increase in indigenous production.

Our exports of goods cannot be increased beyond a point. There is no exportable surplus. India itself is a large market. For most of the last 50 years it has remained a seller's market - with large demands going unsatisfied.

Our trade deficits have largely been fulfilled by NRI remittances and by foreign aids.

Exports have never been able to fully finance our imports.

**With inelastic imports and little export surpluses; devaluation can not help BOT.**

In other words the policy of continuous devaluation has failed to achieve the objective of making the exports exceed the imports, or even to balance the trade.

If this policy has not succeeded for fifty years, how much more time can we give to this policy?

It is necessary to finance - for the next five to ten years, the trade deficit by-

(i) Return of Indian residents' money held abroad;

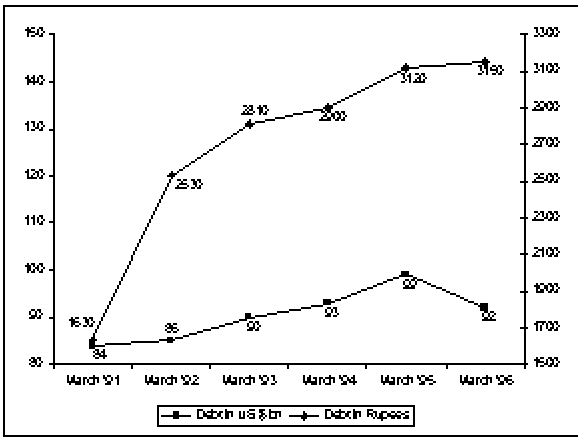
(ii) NRI investments; and

(iii) DFI.

In this much period we must make the economy a low cost economy with high productivity so that our exports can finance our imports.

6.6 Consider the loss in external debt due to devaluation of rupee.

### 6.6.1 INDIAN GOVERNMENT'S EXTERNAL DEBT




6.6.2 During Dr. Manmohan Singh's term as Finance Minister - Debt in US $ has grown from 84 billions to 92 billions (less than 10% increase). Debt in Rupees has almost doubled from 1630 billions to 3150 billions. The reason - Devaluation of the rupee from Rs.18 per dollar to Rs. 33.5 per dollar (in March `96).

This is a telling impact of rupee depreciation.

Assuming a 5% average interest cost on external debt, the additional cost due to devaluation is Rs.72 billions.

$ 92 Bn x (33.5 _ 17.9) = Rs.1435 Bn. Increase in loan due to devaluation.

5% of Rs. 1435 Bn = Rs.72 billion increase in interest cost due to devaluation.

**Devaluation has transferred wealth of Rs.1,43,500/- crores from India to the lending countries.**

The devaluation policy has imposed an increased burden of Rs. 1,43,500 crores on the next government - which finds it impossible to curb the mounting debt servicing costs.

The loss of Rs. 1,43,500 crores is a transfer of wealth to foreign lenders and a read loss to India. It does not get reflected in the budget or counted in fiscal deficit - so people do not consider the loss. It has to be paid in hard cash/exports.

### 6.7 OIL POOL Deficit.

6.7.1 The Oil Pool deficit is because the cost of Crude Oil has increased and the retail price of petroleum products cannot be increased. The deficit is balooning and no viable solution is in sight.

Let us analyse the problem with a "Paradigm shift"

Some of the factors which determine the ultimate petroleum products price are given below.

| Sr. No. | Factors | Remarks | Illustrated Figures |
|---|---|---|---|
| 1. | 1. International Crude price in dollars | Beyond the Control of GOI or IOC. Taken for granted | $ 17 per barrel |
| 2. | Conversion rate of $ and rupee | Taken for Granted that rupee must depreciate for inflation differential | Present Rs.36will continuously fall |
| 3. | Customs, Excise Sales Tax, Octroi | Must keep increasing as government needs more revenue | |
| 4. | Refining costs & margins, Distribution costs and margins | Well within control | |

(**Note**: This is an extremely simplified table emphasising a few key factors in price determination)

Given these parameters, the price of petroleum products has to keep increasing. Petroleum being an important source of energy, chemicals and feed stock for several industries; every price increase translates into general inflation. Government's attempt to control inflation are thwarted by the increase in petroleum price.

6.7.2 Can we Control Petroleum price without causing oil

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| | pool deficit? |
| **No Devaluation, No Oil Pool Deficit.** | Let us challenge the assumption "Taken for Granted"<br><br>Consider a possibility that the conversion rate of Rs. 36/$ were reduced to say Rs.31/$. (The rate before the latest devaluation/depreciation of rupee).<br><br>Entire, current, annual deficit in the oil pool account would be wiped out.<br><br>It may be contended that we cannot revalue the rupee. It is a controversial contention with which we do not agree. However, without discussing the controversy, one can at least agree that the devaluation has caused an increase in crude oil cost by 15% and created the oil pool deficit.<br><br>For last two years, Government has not been able to solve the issue of oil pool deficit. If no devaluation had been made, there would be no problem of oil pood deficit.<br><br>**CONCLUSION**<br><br>If the Government wants that -<br><br>(i) Serious problems like oil pool deficit do not recur;<br>and that<br><br>(ii) Inflation is controlled;<br><br>It must (a) Stop any further depreciation of rupee; and<br><br>(b) Start revaluing the rupee.<br><br>6.8 **Impact on Exports** |
| **Exports get caught up in Inflation - Devaluation Inflation – cycle** | 6.8.1 Several items of exports have very high import content – like diamond and gold jewellery exports. They have little benefit on account of rupee depreciation. With every depreciation, their own costs of purchase go up proportionately and they have to increase the export prices.<br><br>Items like cotton yarn which have negligible direct import content are also affected.<br><br>Where the exporter does not suffer a cost increase, the foreign buyer (who know detailed cost sheets of Indian exporter) forces a price cut. All the benefits go to the foreign buyer. |

Every devaluation causes rise in energy prices, transport prices and a general inflation with a multiplier impact. So some cost increase is felt by all exporters.

Every cost increase/inflation reduces the exporter's profitability and competitive power. Hence he lobbys for further devaluation.

Thus devaluation causes inflation which reduces export competitiveness necessitating further devaluation.

It becomes a self supporting cycle of continuous devaluation and inflation making the country with a high cost internal economy.

6.8.2 Exporters in India have not been able to establish their brand names outside India. They do not have large distribution networks for exports. They cannot undertake extensive advertising compaigns in North America or Western Europe. Low value of rupee incapacitate exporters.

Most of our exports are "low value addition" items.

This situation has emerged because of low value of rupee. A multimillionaire in terms of Indian rupees is a 'no-body' in terms of U.S.$. How can he spend substantial amounts in FX for marketing and distribution!

The only method he has learned for exporting his "commodity" products is by "under-cutting". GOI helps him by devaluing the rupee.

This is not the right way of earning real values by exports.

Real way is by at least having the rupee value equal to its PPP value - facilitating exporters in creating their global establishments. And having an export of goods and services based on values offered and not based on under-cutting.

6.9 **Government Budget**

Devaluation increases the cost of imported product.

**Devaluation causes increase in fiscal deficit.**

Together with customs duties the inflationary impact is multiplied.

Inflation forces the pay commission to increase wages and dearness allowances.

A large part of the benefit to the Central Government in terms of increase in customs revenue is wiped out due to an increase in Government expenses.

This and other cost increases - cause increase in capital and revenue expenses of Central and State governments of India. These result in higher fiscal deficit;

on increase in taxes;

or both.

This causes further inflation.

Another self supporting vicious cycle of devaluation - inflation - devaluation starts.

6.10 **Infrastructure Projects - Foreign Investment**

**Rupee Depreciation Illustration**

Continuously depreciating rupee makes infrastructure projects unviable.

This is one of the reasons why adequate investment is not forthcoming in the infrastructure industry.

This concept is illustrated by an example for a road project.

**Roads**

Consider the example of a new Road Project and examine reasons why private sector investment is not coming in.

| | |
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| 1.1 Assume a road project where the foreign loan component is | \$100 millions |
| 1.2 Interest Payable | 7% p.a |
| 1.3 Loan repayment 20 equal instalments | \$ 5 millions |

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| | 1.4 Company expects a net profit of 10% p.a.<br><br>2.1 Rupee rate in the year July, 1991 Rs.18 per U.S.$<br><br>2.2 Rupee rate in the year June, 1997 Rs.36 per U.S.$ 6 years<br><br>2.3 Annual compounded rate of depreciation of rupee 12.25%<br><br>2.4 If past in projected into future, an investor in India should be prepared for at least 10% depreciation of rupee every year. |

**IMPACT OF RUPEE DEPRECIATION**

| Sl. No. | Loan Balance Opening | Interest $ | Total Payment $ | Deprec. rate Rs./$ | Rs.Mn. payment Rs. | Rs.Mn. payment Rs. | Interest @ 17% | Total payment $ | Rs. Mn. payment $ |
|---|---|---|---|---|---|---|---|---|---|
| 1. | 100.00 | 7.00 | 12.00 | 36.00 | 432.00 | 432.00 | 17.00 | 22.00 | 792.00 |
| 2. | 95.00 | 6.65 | 11.65 | 39.60 | 461.34 | 419.40 | 16.15 | 21.15 | 761.40 |
| 3. | 90.00 | 6.30 | 11.30 | 43.56 | 492.23 | 406.80 | 15.30 | 20.30 | 730.80 |
| 4. | 85.00 | 5.95 | 10.95 | 47.92 | 524.68 | 394.20 | 14.45 | 19.45 | 700.20 |
| 5. | 80.00 | 5.60 | 10.60 | 52.70 | 558.70 | 381.60 | 13.60 | 18.60 | 669.60 |
| 6. | 75.00 | 5.25 | 10.25 | 57.98 | 594.28 | 369.00 | 12.75 | 17.75 | 639.00 |
| 7. | 70.00 | 4.90 | 9.90 | 63.78 | 631.38 | 356.40 | 11.90 | 16.90 | 608.40 |
| 8. | 65.00 | 4.55 | 9.55 | 70.15 | 669.97 | 343.80 | 11.05 | 16.05 | 577.80 |
| 9. | 60.00 | 4.20 | 9.20 | 77.17 | 709.96 | 331.20 | 10.20 | 15.20 | 547.20 |
| 10. | 55.00 | 3.85 | 8.85 | 84.89 | 751.24 | 318.60 | 9.35 | 14.35 | 516.60 |
| 11. | 50.00 | 3.50 | 8.50 | 93.37 | 793.69 | 306.00 | 8.50 | 13.50 | 486.00 |
| 12. | 45.00 | 3.15 | 8.15 | 102.71 | 837.10 | 293.40 | 7.65 | 12.65 | 455.40 |
| 13. | 40.00 | 2.80 | 7.80 | 112.98 | 881.27 | 280.80 | 6.80 | 11.80 | 424.80 |
| 14. | 35.00 | 2.45 | 7.45 | 124.28 | 925.90 | 268.20 | 5.95 | 10.95 | 394.20 |
| 15. | 30.00 | 2.10 | 7.10 | 136.71 | 970.64 | 255.60 | 5.10 | 10.10 | 363.60 |
| 16. | 25.00 | 1.75 | 6.75 | 150.38 | 1015.07 | 243.00 | 4.25 | 9.25 | 333.00 |
| 17. | 20.00 | 1.40 | 6.40 | 165.42 | 1058.68 | 230.40 | 3.40 | 8.40 | 302.40 |
| 18. | 15.00 | 1.05 | 6.05 | 181.96 | 1100.86 | 217.80 | 2.55 | 7.55 | 271.80 |
| 19. | 10.00 | 0.70 | 5.70 | 200.16 | 1140.90 | 205.20 | 1.70 | 6.70 | 241.20 |
| 20. | 5.00 | 0.35 | 5.35 | 220.17 | 1177.92 | 192.60 | 0.85 | 5.85 | 210.60 |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Total | | 73.50 | 173.50 | | 15727.81 | 6246.00 | | | 10026.00 |

For explanations of each column, please see next page.

| | COLUMN EXPLANATIONS |
|---|---|
| **Continuous depreciation of rupee makes infrastructure projects unviable.** | 1. Gives opening balance of outstanding loan in $ millions. Opening loan is $ 100 millions. Annual repayment is $ 5 millions. Opening conversion rate - Rs.36/- $.<br><br>2. Interest payment in $ millions on the reducing balance. Rate 7% p.a.<br><br>3. Total debt servicing in $ millions (interest + $ 5 million loan repayment).<br><br>4. If rupee is depreciated continuously @ 10% per year - the annual rates of rupee, per U.S.$.<br><br>5. Total payments required in Rs. millions; at depreciating rupee (3 x 4)<br><br>6. Total payments required in Rs. millions at constant rupee (3 x Rs.36)<br><br>7. Interest on opening balance (1), in $ if rate of interest were 17%.<br><br>8. Total debt servicing in $ millions (7 + $ 5mn.)<br><br>9. Total payment in rupees millions (8 x Rs.36)<br><br>**OBSERVATIONS** (Para 6.10 continued.)<br><br>1.1 Loan repayment over 20 years and rate of interest is 7% p.a. total payment in 20 years<br><br>Loan $ 100 mn. +<br>Interest $ 73.50 mn.<br>______________<br>$ 173.50 mn. $ 173.50 mn.<br>==========<br>1.2 If rate of rupee is constant @ Rs.36 per dollar; interest rate is 7% p.a., total payments Rs.6,246 mn. |

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| **Continuously depreciating rupee makes infrastructure projects unviable.** | 1.3 If rate of rupee is constant<br>@ Rs.36 per $ interest rate is<br>17% p.a., total payments Rs.10,026 mn.<br>1.4 If rate of rupee keeps falling @10%<br>every year and rate of interest is 7% p.a.<br>total payments Rs.15,728 mn.<br><br>1.5 Assume that the investor is expecting a 10% net profit after payment of all costs, interest and taxes.<br><br>In a depreciating currency every soon the Debt Service payments will exceed its net profits, will cause huge losses and bring entire cash flow to a grinding halt.<br><br>2.1 Continuously falling rupee makes debt servicing impossible and causes the company serious difficulties. Some companies have gone insolvent because of this reason.<br><br>2.2 To say that the investor can build in a 10% depreciation of rupee in his cost of capital - cannot work in many cases. It may work for portfolio investor; or for consumer goods with low payback period. It may not work for infrastructure projects with long pay back periods. Hence they do not get loans in the international markets.<br><br>2.3 Adequate funds are not available within India.<br><br>So do not invest in an infrastructure project.<br><br>2.4 A conservative merchant banker should advise his client considering an infrastructure project in India that -<br>(i) Either ask for guaranteed returns in terms of FX;<br><br>(ii) Or do not invest in India.<br><br>3. Making industrial investment in a country with a depreciating currency is like trying to climb up on an escalator - which is going down.<br><br>People with better alternatives stay away from such countries - especially for low profit, capital intensive projects. |
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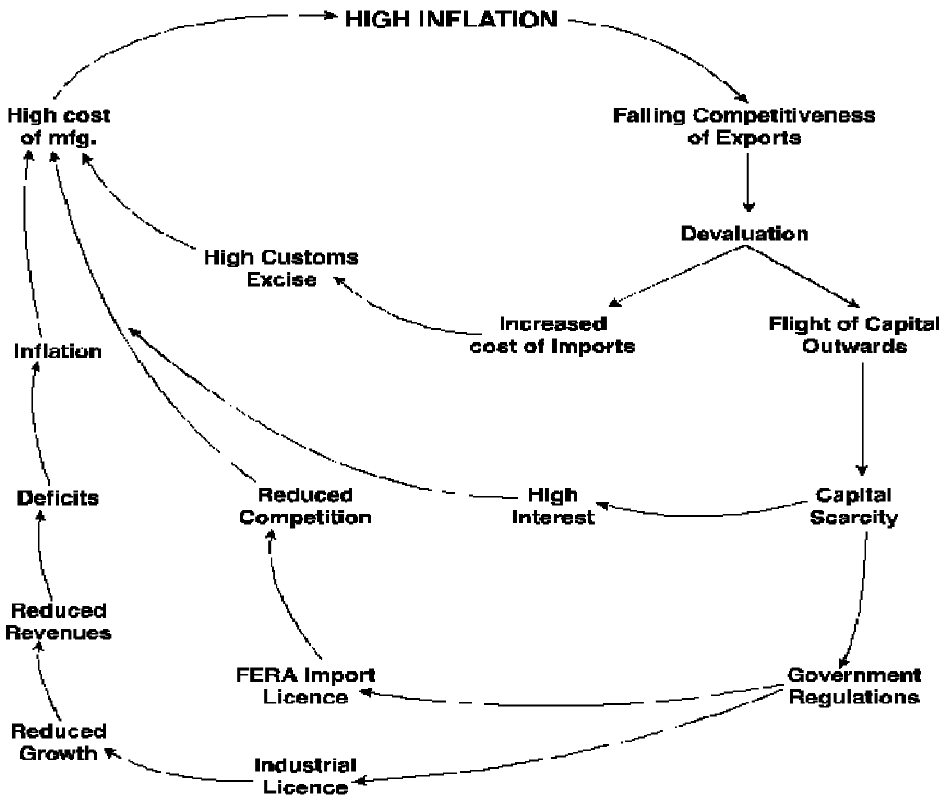
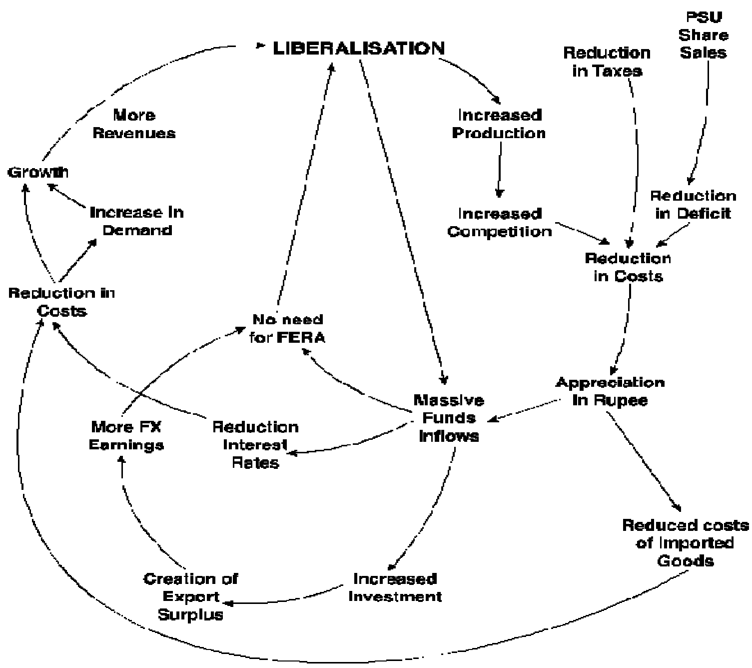
## 6.11 VICIOUS CYCLE




This is past. Pre-liberalisation. Continuous devaluation of rupee has been a key factor in the vicious cycles in the Indian economy.

## 6.12 VIRTUOUS CYCLE




Government has already taken several steps to start a virtuous cycle. Appreciation of rupee will give a strong momentum to the virtuous cycle.

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| **We want FX inflows. But do not want inflation.** | 7. **PARADOX OF BALANCING FUNDS FLOWS**<br><br>7.1 India has a peculiar paradox.<br><br>7.1.1 We cantinue to have a tremendous shortage of funds /capital. Several projects cannot be undertaken or implemented because we do not have adequate funds. We want annual inflow of $ 10 billions.<br><br>7.1.2 We are worried that the convertibility should not, at some stage result in flight of capital outwards. We want to create larger FX reserves.<br><br>7.1.3 At the same time, when the foreign exchange does come in, we are worried that it will cause inflation.<br><br>7.1.4 If too much funds come in, it can cause appreciation of rupee. This can hurt exporters. Reduced exports can hurt Balance of Payments position.<br><br>To prevent appreciation in rupee, RBI intervenes by buying up dollars. This causes flush of money supply. This can cause inflation.<br><br>Absorbing excess liquidity has its own repercussions.<br><br>7.1.5 Summary. We want FX inflows.<br><br>At the same time, we are worried if the funds actually flow in.<br><br>This is not a problem of any ideology or economic theory. It is a plain problem of financial management.<br><br>7.2.1 Government have huge fiscal deficit.<br><br>7.2.2 Government can, probably withdraw from financing PSUs, spending on infrastructure projects and allow private and foreign investments in these projects.<br><br>In 1993-94 when Government did this, there was a reduction In Government spending. However, private spending did not match and there was recession.<br><br>Sanctions for Direct Foreign Investment (DFI) have not materialised into project execution.<br><br>There are still several bottlenecks in implementing new |

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| | projects - whether for Indians, NRIs of Foreigners.<br><br>Bureaucratic red tapism is a major problem. There are several other problems. However red tapism is one serious matter on which Government must act swiftly.<br><br>If the expectations of FX investments do not materialise despite CAC; then it would be a clear loss to the nation.<br><br>7.3 Financial management of FX inflows may be balanced by: directing the inflows to the desired sectors - Annexure III (priority) industries. |
| **With a comprehensive strategy it is possible to have FX but avoid inflation.** | 7.4 Export of goods like foodgrains and cotton cause inflation by reducing supply of goods.<br><br>FX inflows on account of investments cause inflation by increasing money supply.<br><br>Yet we cannot reduce FX inflows.<br><br>In the short run, the problem has to be met with by –<br><br>Reducing inflation,<br><br>Reducing cost by –<br>(i) Reducing customs and excise rates<br>(This is also wanted by World Trade Organisation)<br><br>(ii) Allowing minor appreciation in rupee;<br>(iii) Allowing import of goods of basic necessity and controlling market prices by supply side management;<br><br>(iv) Reducing administered prices;<br><br>(v) Reducing fiscal deficits;<br><br>(vi) Directing DFI and Indian investments to replace Government capital expenditure.<br><br>One way of allowing large FX inflows, building up FX reserves and not permitting inflation is discussed below.<br><br>The growth in money supply may be controlled by the following method. |

Net BOP surplus, if any should be set off by appropriate reduction in Budgetary deficit. Thus, if during 1997-98, the net BOP surplus is, say, U.S.$ 6 billions, the budgetary deficit should be reduced to zero.

If one can achieve the complex target of directing FX inflows and domestic savings towards replacing Government expenditure; then the target of achieving balance in funds flows can be achieved.

Appropriate change in the policy of marketing PSU securities can help. However, this subject may not be discussed in this presentation.

In the long run, incremental investments should create production surpluses at competitive costs. This along can permit exports and relieve India from constant FX shortages.

If FX inflows are frittered away in any uses which do not increase production; then we will be inviting trouble.

For the purpose of directing the investments, we must create appropriate market incentives and cut out bureaucratic delays.

**Summary**

There are a lot of economic theories - which cannot be discussed in this paper. However, the purpose of this note is to suggest that it is possible to work out a comprehensive economic plan to make a success of convertibility and appreciation of rupee.

8. **VOLUNTARY DISCLOSURE OF INCOME SCHEME & FERA**

8.1 As discussed earlier, Indians have transferred their wealth abroad. To a large extent, Government has not been able to do anything about it.

Even after this experience for 50 years, Government has not accepted futility of legal restrictions. Creation of favourable economic and legislative environment is the only way to bring in FX.

Instead, probably, it is planned - to continue the same law

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| | which makes retaining wealth abroad a punishable crime.<br><br>As per newspaper reports –<br><br>(i) RBI has recommended that sections 8 and 9 of FERA should not be repeated in FEMA.<br><br>(ii) Revenue Secretary is reported to have told the press that FEMA will have all the restrictions existing in FERA.<br><br>Our submission - if these sections with draconian powers to the ED are retained in FEMA, it will be a clear signal that Government has not accepted a "paradigm shift." It continues the same old approach. No significant amounts will come in the country.<br><br>8.2 What is the VDIS scheme?<br><br>From all official utterances, Government simply wants revenue. In collecting the revenue, if the declarant finds FERA to be an irritant, give him an immunity so that he may come forward.<br><br>This is not an "Amnesty" scheme. You are not prepared to pardon any one who is proved to be guilty. |
| **VDIS does not give "Amnesty".** | You are not even prepared to pardon any one accused of being guilty. Not even a person against whom an inquiry is started.<br><br>You only want to give immunity to someone whom you have not been able to catch.<br><br>There is a chance of one in a million that Government will ever be able to catch a person who has not been caught so far.<br><br>Why should he come forward?<br><br>He know that the immunity is transparently inadequate. And the same old laws will continue.<br><br>8.3 The VDIS scheme only provides that the declaration made under the scheme cannot be used as evidence. Period. It does not at all say that the offence covered by the declaration will be pardoned. (As far as FERA is concerned.) RBI has asked people to make "applications" in form FAD1. |

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| | An "application" means, the discretion whether to permit and regularise the foreign investment or not remains with RBI. FAD1 also should be a "declaration" and not an "application". On filing of the from, the "pardon" or regularisation should be automatic. RBI should only have discretion to determine whether to permit continuation of the investment or not.<br><br>A scheme leaving discretion to RBI in the year 1986 had failed. We recommend:<br><br>(1) As a temporary measure - the VDIS scheme should be amended. The offence under tax & FERA converting the amount declared should be totally pardoned.<br><br>(2) As a permanent measure: Make a policy declaration that within a time bound programme, FERA will be scrapped. FEMA will not have section 9, 16 and 18 of FERA.<br><br>9. **ENFORCEMENT DIRECTORATE**<br><br>9.1 Enforcement Directorate had to deal with powerful violators of the law like smugglers and havala racketeers. (Hereinafter in this presentation referred to as smugglers only). These smugglers had the powers to bribe the highest authorities; to hire best lawyers; to eliminate evidence.<br><br>Those honest ED officers who wanted to enforce the exchange laws could never succeed. Hence they wanted more and more powers - ultimately crossing the limits of civilised democracy.<br><br>9.2 When some one transfers funds to or from India by havala transaction; the chances of some one getting caught in the Act are less than 10%. In 90% of the cases of havala transactions, the ED has no direct evidence. |
| **ED cannot effectively punish the powerful smugglers.** | The havala agent's diary and similar indirect references - are the only indirect evidence available to the ED.<br><br>The easiest technique they have employed to prove their allegations and get the accused booked is - use or threaten to use third degree measures. The accused will sign any confessional statement that the ED officers will insitst. Use this confession together with other indirect evidences and |

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| | punish the accused.<br><br>Now, it is a well known secret that no ED officer would risk his life by being even rude to a smuggler or his accomplice - if ever a real smuggler is caught. There is no question of using third degree measures against the smugglers.<br><br>So these power are exercised only against the businessmen who may be caught by some chance.<br><br>9.3 In the Jain Havala Case, Supreme Court has ruled that a third person's diary is no proof against the accused. With this decision, whatever thin legal support ED had so far, is gone.<br><br>In future, all accused persons will use this judgment in their favour and the ED will not be able to do anything.<br><br>Under Income-Tax Act, similar situation had arisen. Under Section 52 of the Income-tax Act, in case of sale of immovable property at lower than market price, department could levy additional tax. Supreme Court ruled that "passing of cash amount" must be proved to levy additional tax. Actual passing of cash could never be proved. Ultimately, the whole of S.52 had to be deleted from the Act by an amendment through Finance Act, 1987.<br>A similar future awaits the penal proceedings under S.50 of FERA.<br><br>As long as you do not scrap Sections 9, 16, 18 under FERA, you are continuing a situation where –<br><br>(i) The smuggler will never be punished as ED officers do not have the courage and capability to challenge the real smugglers;<br><br>(ii) All those people who cannot be forced to "confess" - will not be punished;<br><br>(iii) Only ordinary individuals who can not prevent / withstand tortures; and who cannot hire competent lawyers will be punished under FERA!!!<br><br>Can a civilised democratic country continue such unfair situation! |
| **Sections 9, 16 and 18 of FERA should be scrapped.** | |

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| | 9.4 Let us consider some instances of ED excesses.<br><br>Names of the parties involved are not given. We shall not be able to give any further information than that given in this report. |
| **Exporters suffer due to ED.** | 9.4.1 A young man started the business of exporting goods. Initially he exported goods to closely known relatives and was very successful. Then an NRI met him and enticed him for substantial exports on credit. [ We have cut out the long story ] The Indian exported goods and the sale proceeds were never received. The case was handed over to the ED.<br><br>The Indian exporter fully co-operated with ED and gave full information. The NRI's Indian relative who was fully involved in the transaction was arrested by ED. Full information was obtained by ED. After a week the defaulter was released on bail who fled abroad. The Indian could not pay to his suppliers as he had not received his sale proceeds. He sold away his large factory, shifted to a small place and paid off a large portion of his debts. This was not sufficient. He is now planning to sell some of his inherited properties to pay off the remaining debts.<br><br>Since the young man had suffered, he could not take things lying low - as other businessmen normally do. He complained to the Economic Intelligence wing of Government's agencies. After a long time, the EIW advised him that - the foreign importer had joined a Middle-East based NRI mafia. He has duped several other exporters. In the interest of his own safety, the young man should stop pursuing the case.<br><br>All this is Government's information.<br><br>And yet, the exporter is not relieved of the accusation that - "he has violated S.18 of FERA by not bringing in the export proceeds within 180 day."<br><br>He still remains afraid of ED and cannot concentrate on business. He has no money left to spend after the lawyers and other related costs. There is no salvation for him.<br><br>9.4.2 Mr. and Mrs. A purchased a residential flat from an NRI. They paid by cheque, the purchase price. After some time, Mr. A died. After a few years, the bank - where NRI |

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| **Innocent transactions are termed" violations" under FERA.** | had his bank account, underwent audit. Information reached the ED that some resident had made payment to a Non-Resident. This is violation of S.9(1)(a). No Indian resident can make any payment to a Non- Resident.<br><br>Notification No. FERA 152/93-RB dated 26th May, 1993 permits the NRI to sell his immovable property without any specific permission from RBI. He may receive the sale proceeds.<br><br>Paragraph 13A.6(b) of the RBI manual (1993 edition) permits the NRI's bank to credit the sale proceeds to the NRI's bank account. (In the earlier edition, this item was specifically permitted. Now it is covered by a broad group of permissible credits.)<br><br>The ED served a notice on the widowed, old lady Mrs. A that she had violated the provisions of S.9 of FERA.<br><br>They also said that the provision of S.9(4) will be of no help to her.<br><br>In simple words and cutting out technicalities - The NRI owner is permitted to sell, the NRI's bank is permitted to credit his account but the resident buyer is not permitted to make payment to the NRI.<br><br>Ultimately, Mrs. A had to pass through several hassles and costs before she could breath easy.<br><br>If S.9 permits such an interpretation - and RBI confirms that it does; then such a section has to be abolished.<br><br>All perceived losses to the economy pale before the Government terrorism on the innocent and weak people in the name of S.9.<br><br>9.5 **Human Right Violations by Enforcement Directorate**<br><br>Several Governments in the world act as terrorists and commit gross violations of human rights.<br><br>U.S.A. did it on Vietnam and several other countries. |
| **For all human rights violations by ED, Finance Minister is** | U.S.S.R. did it in Afghanistan & several other countries. Iraqi Government continues its tormentation on Kurdish people |

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| **morally responsible.** | even today.<br><br>Indian Government commits its human rights violations through the enforcement directorate. This is one department which is convinced that-<br>Once it makes an allegation against anyone –<br><br>(i) That person looses all his fundamental rights under the Constitution; and<br><br>(ii) E.D. can use third degree tortures; and cause other harassments to the accused.<br><br>For every crime that an enforcement officer commits against the Indian citizens; the Finance Minister is morally responsible. And several ED officers commit several human rights violations every day.<br><br>Late Prime Minister Shri Lal Bahadur Shastri resigned from his post of Railway Minister - owning up the responsibility for a railway accident.<br><br>As a conscientious minister that you are, you may be embarrassed by all the violations that your officers do.<br><br>The alternatives available today may be:<br>(i) Wind up the whole of the present ED.<br>OR<br>(ii) Remove all powers of harassment & prosecution from the ED, Scrap FERA, and<br><br>(iii) Institute criminal action against those officers of ED who indulge in human rights violations.<br><br>(iv) Ensure the FEMA & Anti - Money Laundering Laws will be strict & yet civilised laws.<br><br>9.6 **Enforcement of FEMA ED.** |
| **People expert in international finance should constitute new** | An agency which will enforce FEMA and Prevention of Money - Laundering laws should have a capability of detecting money laundering & effectively preventing the same. It should also have people experts in FX dealing, derivatives and options. These are sophisticated modern financing instruments. |

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| | Enforcement Directorate gives a normal perception of - people who can only use brute force against small businessmen. They are ineffective against the smugglers. They may prove to be ineffective against FX gamblers & derivatives gamblers.<br><br>An entirely new department should be created with people trained in sophisticated modern financial instruments. These people should be given specialised training in dealing with financial crimes. This department may be organised and be ready by 31st December, 2000.<br><br>ED may be wound up on 31st December, 2000.<br><br>To avoid infection of ED practices into the new department, not a single person may be transferred from the ED to the new department. ED should simply disappear from the face of India.<br><br>10. **REVALUING THE CURRENCY**<br><br>THE REASON FOR OPTIMISM<br><br>10.1 India is today in a position where it can take some risks. It can test new and radical ideas. All ideas will be challenged by some people.<br><br>In Economics, no idea is the ultimate right or wrong.<br>It is only that in certain societies, at certain times, given the commitment and work put in by the society, some ideas work; and some ideas do not work.<br><br>One idea, economic theory, or strategy may be successful at one time; and a failure at another time.<br><br>Success of an idea at a time, sometimes makes people prisoners of that idea. Many successful people are unable to come out of their successful doctrines even after the times have changed. |
| **BOP position permits appreciation of rupee** | 10.2 As discussed earlier in (paragraph I 2.1.2, page 11) the Balance of Payments position is in our favour. With consistent liberalisation, there is an inward flow of funds. The market forces are pushing the rupee up. Based on demand and supply equilibrium, rupee value should go up. If the rupee is pushed up too much and if the inflows are not |

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| | sustained; then there can be a crash. This is what has happened with many countries. Their experiences should not frighten us. Their experiences teach us the lesson of moving cautiously but firmly.<br><br>10.3 Mexico allowed large inflows of short term funds and merrily spent on consumption goods. Country invited the trouble. So the fact that Mexican currency & economy crashed, should not worry us. We are acting far more prudently.<br><br>10.4 We have to ensure that the funds that come in are long-term funds. There should be more emphasis on Direct Foreign Investment (DFI) than on the speculative financial institutions' portfolio funds. Experience internationally (latest case of Thailand) have shown that Institutional investments are also hot money. We do not think they should be given any tax concessions.<br><br>10.5 Funds coming in should help in creating exportable surpluses and BOP surpluses.<br><br>We will definitely need to direct investments in our country until sustained exportable surpluses are created.<br><br>Any talk of not directing the investments in desired areas may not help us in achieving sustained exchange stability. But this is another issue.<br><br>10.6 We can create an economic position that –<br>(i) Indian residents have faith in India. They retain their wealth in India and bring in the black money that they have held abroad. (This will never be achieved by legal force but will be extremely easy by economic attractions.)<br><br>(ii) NRIs have faith in India and they pump in more funds.<br><br>(iii) Foreigners will automatically follow a market which is attractive.<br><br>The order of priority should also be as given above.<br><br>10.7 These funds inflows will help appreciating rupee.<br><br>Allow an annual appreciation of rupee in the range of 2% to 5%. |

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| **Several economic forces together can transform the economy and start a virtuous cycle.** | This will build tremendous confidence in India attracting even more funds.<br><br>10.8 At this stage, market all the PSU shares, allow huge investments in infrastructure projects, have a proper tax amnesty scheme.<br><br>Substantial funds will be diverted to Government by PSU sales. More private investments in infrastructure will take the burden off the Government shoulders. Pay off your internal & external debts.<br><br>Reduce debt servicing costs. Reduce fiscal deficits. Reduce inflation. Increase the real value of rupee. Let the rupee appreciate further by 2% to 5% every year.<br><br>With massive investments in industry and agriculture, with improvements in productivity because of competition & reduction in regulations; there should be export surpluses.<br><br>When exports start financing 100% - of imports; it will be a time for removing even the directory regulations on FDI.<br><br>10.9 You have already taken several steps to start the virtuous cycles. Appreciating rupee will be a strong boost to the virtuous cycles.<br><br>Because of appreciation in rupee, cost of imported products including crude oil - in terms of Indian rupees will fall. This will be a strong help to you in controlling inflation. It will also help in solving the oil-pool deficit - problem. Such a price reduction will not cause recession. It will only boost - production.<br><br>10.10 This will be a challenge to the - traditional economic theory that inflation and growth go together. We are in a position where we can have price reduction and growth.<br><br>10.11 The fallacy in the traditional theory is very simple. |
| **It is wrong to say that inflation and growth go together.** | Basic theory is that more investments should cause more production and growth. When you have limited funds, you "create" funds by budgetary deficits. This creation of funds causes inflation. Hence the theory has been that - "Inflation & growth go together." |

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| | We are in position to attract more investment and funds by causing small appreciation in rupee. There can be more funds, more imports at lower prices. And hence there can be growth with reduction in prices.<br><br>10.12 Caution<br><br>Possible Dangers in this policy<br><br>10.12.1 Substantial appreciation in rupee can cause large increase in the demand for imported goods and can create a BOP crisis.<br><br>10.12.2 Appreciating rupee will hurt exporters & reduce exports. |
| **Appreciating rupee is not a cake walk.** | 10.12.3 The lobby that is interested in seeing our currency value to be as low as possible; will pay several games to force us a devaluation. Easiest game for them will be to persuade a few of our competing countries into devaluing their currencies.<br><br>**Response - Past**<br><br>10.13 The fear of the first two dangers have always prevented us from allowing any appreciation - in rupee. And we have always selected the easy way out - Depreciate.<br><br>**Response - Future** |
| **We cannot go on taking easier options.** | 10.14 These fears can be answered only in the following manner:<br><br>10.14.1 First we have to stop depreciation of rupee. Stabilise rupee. And appreciation should be very small.<br><br>10.14.2 Build large reserves and keep paying off short term or costly<br>loans.<br><br>10.14.3 Realise that the problem is complex and calls for extreme caution. This needs building a consensus amongst Government, industry, and the profession. Several strategies may be discussed in depth and then the progress may be |

made.

For exports, please see paragraph II 6.8, page 46.

10.14.4 For international lobbies - we have to create a lobby of India, China, Russia, Indonesia, Malaysia, Thailand, Phillipines, Brazil and similar countries. This is a large issue, beyond the scope of the present paper - and at the same time needing urgent commitment.

**SECTION II - RADICAL APPROACH**

**SUMMARY**

11. **BRIEF SUGGESTIONSTIME TABLE**

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| 1. Open up Trading of Indian Companies' GDRs & ADRs on Indian stock exchanges. | 1st April, 1999 |
| 2. Establish advance institutional set-up for International Finance Centres in India. | 1st April, 1998 |
| 3. Establish advance institutional set-up for International Trading Centres in India. | 1st April, 1998 |
| 4. When these institutions are ready, open up India for international finance & trading – probably by | 31st December, 1999 |
| 5. Establish Regulatory and market intelligence systems for Derivatives and Options | 31st December, 1997 |
| 6. Abolish the Enforcement Directorate's power to arrest without warrant. | 15th August, 1997 |
| 7. Institute criminal action against those officers of ED indulge in violations of human rights. | 15th August, 1997 |
| 8. Create a modern, well trained regulatory machanism to prevent FX gambling. | 31st December, 1998 |
| 9. FIPB and RBI may consider proper | |

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| | direction of funds for balancing Funds for balancing Funds flows. | 15th August, 1997 |
| | 10. Stop any further depreciation or rupee | 15th August, 1997 |
| | 11. Let the rupee appreciate if BOP causes apprecation - upto 5% per annum. | 15th August, 1997 |
| | 12. Have an Asian Group of Nations consisting of India, China, Russia, Indonesia, Thailand, Phillipines, etc. | |
| | 13. Amend the VDIS and grant proper amnesty. | 15th August, 1997 |
| | 14. Make Rupee fully convertible | 31st December, 1999 |
| | 15. Lift all restrictions on imports & exports without warrant. | 31st December, 2000 |

**SECTION : III**
**FEMA**

**Page Nos.**



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| | 1. **FEMA AND RBI**<br><br>1.1 **Administrative Structure under FERA**<br><br>1.1.1 **PAST**<br><br>When we are drafting a new law, let us examine some aspects fundamentally. RBI has been able to remain above the prevalent standards of morality in India because of - inter alia, the following structure in administering and enforcing FERA.<br><br>(i) RBI does not have any powers to impose penalty. In fact RBI does not have the responsibility to enforce the law. That was entirely left to the Enforcement Directorate. When there is a fear of prosecution, the culprit will try all the resources at his command - including bribing - to get a decision in his favour. This is "not applicable" as far as RBI is concerned.<br><br>(ii) Before June, 1991 there was not much to Administer FERA. There were not many decisions to be taken.<br><br>Almost everything was prohibited under FERA. |
| **RBI could remain" above board" because it did not have powers to penalise, or to take important decisions.** | Certain important decisions like "Foreign Collaborations' ", "External Commercial Borrowings" (ECBs) and "Joint Ventures Abroad" were taken by different ministries. Once major decisions were taken, RBI was to only look after the follow-up action.<br><br>(iii) Exchange Control Department (ECD) of RBI was not meeting the citizens of India. Neither the applicants nor their |

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| | representatives were allowed to meet ECD officers.<br><br>People had less reasons to try to bribe ECD officers and there was little direct contact between the two.<br><br>1.1.2 **PRESENT** |
| **Now RBI takes important decisions. If power to penalise is granted, RBI can be like the rest of India.** | Now RBI has started taking important decisions on foreign collaborations, joint ventures and ECBs. And the officers have started meeting the applicants. And some of them have started being like the rest of India.<br><br>If and when the power to penalise will be granted to RBI, there may be no difference between the culture of RBI and the culture of an ordinary Indian.<br><br>This potential is real and has to be considered while drafting FEMA.<br><br>One cannot even imagine the Central Bank of a country - which will be managing our foreign exchange and ruling over the Banking industry - not being above board.<br><br>1.2 **Administrative Structure under FEMA**<br><br>**FUTURE**<br><br>Following principles may be considered while drafting FEMA.<br><br>1.2.1 So far, we had kept FX on a high pedestal. It was the ultimate need of Indian economy. It was scare and anything could be sacrificed fore FX.<br><br>1.2.2 Because FX was on a high pedestal, ECD at RBI was on a high pedestal. Vast powers were given to RBI. FERA is not really a law where Parliament has legislated a full bodied law. It is a law which states that “nothing can be done without a permission under FEMA”. And the rest of the law making has been delegated to Government of India and RBI. They issue notifications and circulars and make the law.<br><br>1.2.3 We must accept that FX need not be kept on a high pedestal. Growth of Indian economy is more important and cannot be sacrificed in the name of FX. And there are better ways of growing the FX reserves.<br><br>1.2.4 ECD and RBI are like any other department having |

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| | statutory powers - say Income-tax department. |
| **FEMA should not be a law made and changed through circulars and notifications.** | 1.3 **Drafting the Law**<br><br>Hence a full-bodied law with all the guiding principles incorporated within the law must be presented before the Parliament. Law making should not be delegated by Parliament to the officers drafting and issuing notifications. Even rules must be considered and passed by the Parliament.<br><br>GOI and RBI should only have the powers to issue "clarifications" and to "remove difficulties" by issuing notifications and circulars within the frame work of law and rules passed by the Parliament. |
| **Appellate Tribunal under Law Ministry should hear appeals against RBI decisions.** | 1.4 **Appellate Tribunal**<br><br>There should be an Appellate Tribunal to consider the bonafides and correctness of ECD's decisions. There can not be any statutory administrative authority's decision that is "final and binding" and withou appellate authorities.<br><br>This tribunal should work under the Law Ministry and should be independent of the Finance Ministry. This is such an important issue that any compromise on this is bound to deteriorate the standards of justice give by the Tribunal.<br><br>If a judicial authority like Appellate Tribunal work under Finance Ministry, when promotions and transfers of Tribunal members are decided and affected by the administrative ministry, a "conflict of interests" is bound to develop. When this develops, most human beings succumb to the material temptations. |
| **Business decisions should be left to the businessman.** | 1.5 **Business Decisions**<br><br>The power to take business decisions should be left to the businessman.<br><br>Under Income-tax, when a businessman spends any amount - whether on capital or revenue account; the officer has no powers to ask why this amount was spent. He can only ask whether the amount was actually spent.<br><br>There is no reason why one should grant the ECD officers a power to interfere with the business decisions of the |

businessman.

When rupee is made fully convertible - say by the year 2000 - there will be no scope for RBI in interfering with any business decisions.

Central Bank in some countries have been able to maintain their dignity because their currencies are fully convertible. The Central Bank do not have to get into mundane administrative matters. They remain as the authorities taking macro level policy decisions.

1.6 **Authorised Dealers** -- A large portion of the work should be left to the bankers. And they should not have much discretion. They should only act as bankers and simply grant remittances of foreign exchange within the prescribed limits.

**Summary**

1. FEMA - Act and Rules should be full-fledged legislations.

2. There should be an Appellate Tribunal above ECD which is independent of RBI and Finance Ministry.

3. RBI should have no powers to interfere with the business decisions.

2. **FEMA & ED**

**Enforcement under FERA**

2.1 Enforcement Directorate has been placed in an unenviable position. It has been given an impossible task.

As discussed in para II 3.2, page 30, the artificial restrictions through import licensing, customs and FERA have created huge market forces for smuggling and havala transactions.

The financial power, political power and the muscle power in that business is so huge that ED officers are helpless in enforcing the law. Any honest officer would be frustrated. There have been cases of officers who are forced to accept the dictum “If you can’s beat them, join them”. All their anger and frustration is vented out on the small people who cannot fight back.

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| | It is not the department personnel's fault if they are what they are.<br><br>At the same time, the culture in the ED has been so established that these people can not be given enforcement powers. If allowed, they will continue human rights violations.<br><br>They cannot be retrenched also. Russia has experimented with retrenchment of large number of military personnel - with disastrous effect.<br><br>Hence enforcement directorate people may be transferred to such posts where they have no powers to harm citizens of India and yet they can continue to work and earn salary. If some / many of them go on voluntary retirement, that may be accepted. |
| **ED can enforce FEMA only if FEMA is market friendly.** | 2.2 It has been established that -<br><br>(i) Any amount of legislation cannot fight market forces;<br><br>(ii) Giving vast powers to the enforcement authorities does not in any way solve the problem. In fact, if create its own set of problems.<br><br>The solution - which you have already started implementing is:<br><br>Make the laws market friendly.<br><br>If you make rupee fully convertible, you will break the backbone of the smuggling and havala business. Then majority of the people will be law abiding and those few who violate the remaining law, can be dealt with effectively by any good enforcement agency.<br><br>2.3 **Enforcement under FEMA**<br><br>An entirely new enforcement department should be created. This department may enforce the FEMA and Anti-Money Laundering Law. The department may be manned by ex-foreign exchange dealers from banks, chartered accountants, Lawyers and other professionals who have had international exposures. |

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| **A broad minded, humane commission can settle majority of cases.** | 2.4 **Settlement Commission for FERA**<br><br>There are cases of violations of law where the Government would like to punish the guilty.<br><br>There are other cases where the Government may be more concerned about compensation. A majority of the cases may be simple technical violations. For these cases, a settlement commission like the settlement commission under Income-tax Act may be established.<br><br>Thousands of cases of technical violations of FERA – which are never brought to conclusion for years together, may be compounded by the settlement commission on imposition of nominal penalties. The commission may also have powers to completely pardon technical cases.<br><br>**Summary**<br><br>Enforcement Agency can be effectively useful for the nation if FEMA tries to only regulate market forces and not to prohibit market transactions. New international finance environment needs entirely professional people to man the agency. A settlement commission with clear targets & powers can reduce the burden on overloaded judiciary.<br><br>3. **CONVERTIBILITY AND INCOME-TAX**<br><br>3.1 Our Income-tax Act is not equipped to meet with complete convertibility of rupee.<br><br>Consider a few examples.<br><br>3.1.1 With full convertibility, an Indian Resident - Say, Mr. I can send his savings abroad and lend the same to his NRI relative - Mr. N. This loan can be interest free.<br><br>Mr. N can place the funds in FCNR or NRE accounts in India and earn tax free interest.<br><br>Mr. I can borrow funds if required on the security of the deposits in the name of Mr. N.<br><br>This would not amount to Money laundering. Each |

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| | transaction would be perfectly legal under the existing Income-tax Act and future FEMA. |
| **Before full convertibility if I.T. Act is not amended, Anti-Money Laundering Law will not be effective.** | 3.1.2 A consultancy firm - Say M/s. CF is earning fees from abroad. Its directors etc. have to travel abroad for their work. At present 100% of their fees are taxable.<br><br>After convertibility, M/s. CF can open a consultancy company in any tax haven. The Indian directors can also be directors of the tax haven company. For all the services rendered abroad, fees may be charged by this foreign company. There will be no taxable income in India.<br><br>This company may never declare a dividend. The Company may pay all foreign travel and other expenses of its directors. The tax haven company can even give loans to the Indian company and charge interest on the same. The Indian company will claim the interest as a deductible expenditure - Foreign company will take the funds abroad after paying 10% or 20% tax depending upon the tax haven in which it is based.<br><br>Foreign company can even give loans by ECB and claim tax exemption.<br><br>3.2 Anti-Money Laundering law may help only to some extent.<br><br>3.3 The whole structure of the Income-tax Act pertaining to NRI taxation, Foreigners' taxation and Double Tax Avoidance needs proper reorganisation. There are serious anomalies. We will submit a separate paper on this subject.<br><br>We do not, for a moment, suggest that because of these difficulties, FERA liberalisation should be delayed. However full convertibility may take one to three years. New Income-tax Act may be drafted before this period.<br><br>The following issues may have to be considered –<br><br>(a) Can we permit a situation allowing tax free accounts to non-residents and taxable accounts to Indians? This will only cause routing of funds through NRIs.<br><br>(b) Should we tax Indian residents' world income or should we tax only the income accruing & arising in India. |

(c) Should we introduce 1egislation similar to the taxability of "Controlled Foreign Companies' tax" in U.S.A.

**Summary**

Present Income-tax Act and the Expert Group's report on simplification have not considered implications of globalisation. This issue will need a separate expert committee to work on it.

**CONCLUSION**

FERA has served its purpose in the past.

A new law - FEMA which is in line with modern democratic principles which supports globalisation of India be introduced.

RBI should not have the powers to interfere in business decisions of the businessmen.

Enforcement Directorate should not be allowed human rights violations.

Depreciation of rupee should be stopped.

Whenever BOP situation permits, a 2% to 5% annual appreciation of rupee should be allowed.

Rupee should be made fully convertible by 31st December, 1999.

All restrictions on imports and exports should be done away with from 31st December, 2000.

A comprehensive economic policy can be worked out which permits substantial inward flow of funds, does not cause inflation and permits growth in GDP and exports.

**FOR BOMBAY CHARTERED ACCOUNTANTS' SOCIETY**
*President*

**ASHOK DHERE**