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Foreign Exchange and Smuggling Activities in Indian Context

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ABSTRACT

The paper examines the evolution of foreign exchange regulation in India, tracing the transition from the restrictive Foreign Exchange Regulation Act (FERA) of 1973 to the more liberal Foreign Exchange Management Act (FEMA) of 1999. The paper analyses the objectives, provisions, and implications of these acts on India's economic policies, enabling greater integration with the global economy. Additionally, the paper investigates the phenomenon and historical background of smuggling activities in India, covering various periods and regimes, and demonstrating the impact of smuggling on the country's foreign exchange reserves and economic stability. The paper underscores the role of smuggling in depleting foreign exchange reserves, skewing economic indicators, and affecting government revenue through evasion of taxes and import duties. The paper also outlines the measures adopted by India to curb smuggling, such as enhanced customs enforcement, technological innovations, stringent laws, and international cooperation initiatives. Despite the challenges, the paper acknowledges the intricacy of smuggling and the government's continuing efforts to reduce its negative effects on foreign exchange and the overall economy.

Keywords: *FERA and FEMA Transition, Regulatory Framework, Smuggling in India, Foreign Exchange Management, Indian Economy.*

I. INTRODUCTION

Foreign exchange plays a pivotal role in the international economy, facilitating trade and investment between countries. This market operates 24 hours a day, five days a week, and is characterized by its decentralized nature. Foreign exchange rates fluctuate continuously, influenced by various factors such as economic indicators, geopolitical events, and market sentiment.[3] In the realm of international finance, foreign exchange serves as a fundamental tool for businesses, governments, and individuals to hedge against currency risks and capitalizes on currency movements. It is the largest financial market globally, with a daily trading volume that

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[3] Hu, Min, et al. "Macro factors and the realized volatility of commodities: a dynamic network analysis." *Resources Policy* 68 (2020): 101813.

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surpasses trillions of dollars, making it a focal point for investors, speculators, and financial institutions worldwide. As this market's complexities continue to shape global finance, understanding the mechanics of foreign exchange is crucial. According to renowned economist Richard M. Levich, "Foreign exchange is the heart and soul of international finance, and a comprehensive understanding of it is essential for participants in the global economy".[4] Foreign exchange is also abbreviated as Forex or FX. Different countries have different currencies and Forex converts the currency of one country into another. Foreign exchange is the process of converting the legal tender of one sovereign state into that of another at the prevailing exchange rates.[5] Foreign exchange is also required for international trade. For example, when India is trading with the United States both INR and USD are involved. If India is importing from the United States, it needs to pay in dollars, and if US is importing from India it will pay in rupees. Foreign exchange plays a pivotal role for investment in another country.[6]

However unbalanced fluctuations in foreign exchange can lead to smuggling activities for several reasons. When there is a significant difference between the official exchange rate and the black market or unofficial exchange rate, individuals and businesses may engage in smuggling to take advantage of this price differential. They can buy foreign currency at the official rate and sell it at a higher rate on the black market, making a profit. Smuggling often involves the illegal import or export of goods to avoid taxes, tariffs, or import restrictions. A stronger foreign exchange rate can increase the profitability of such activities, as the value of goods in foreign currency terms may be higher, making it more lucrative for smugglers. Smuggling can be a way to launder money obtained through illegal activities. In regions where there are significant economic disparities between neighboring countries, people may engage in smuggling as a means of survival. A stronger foreign exchange rate can create a price differential that encourages smuggling, especially in border areas and it also provide an opportunity to convert ill-gotten gains into foreign currency, making it easier to move money across borders and legitimize it through trade activities. Foreign exchange is traded virtually 24x7. The foreign exchange financial market is the most liquid in the world, as it involves the exchange of trillions of dollars of transactions every day. Traders in this market involve several institutions including the government, central banks and commercial banks, institutional

[4] Levich, Richard M. *International financial markets*. McGraw-Hill/Irwin, 2001.
[5] Alotaibi, Khaled. "How exchange rate influence a country's import and export." *International Journal of Scientific & Engineering Research* 7.5 (2016): 131-138.
[6] Bhasin, Niti, and Vartika Khandelwal. "Relationship between foreign institutional investment, exchange rate and foreign exchange reserves: The case of India Using ARDL bounds testing approach." *International Journal of Financial Management* 4.2 (2014).

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investors, forex agents, individuals, and other businesses.[7] However, weak regulatory and enforcement mechanisms can make it easier for smuggling activities to thrive. If authorities do not effectively monitor or control foreign exchange transactions and cross-border trade, it can facilitate smuggling. To combat smuggling activities driven by changes in foreign exchange rates, governments often implement measures such as tighter currency controls, trade regulations, and border security. Additionally, addressing the underlying economic disparities and incentives for smuggling can help mitigate this issue.

II. Evolution of foreign exchange

The origins of currency trading can be traced back to the ancient civilizations of Greece and Egypt, where molten silver and gold coins were used as mediums of exchange. The value of these coins was determined by their weight and size, reflecting the intrinsic value of the metals. However, this system changed with the rise of the Roman Empire, which centralized the minting of coins and established a government monopoly on currency trading. This monopoly-like structure has persisted until the present day, with central banks having the authority and responsibility to regulate monetary policies. Another significant change in the history of currency trading occurred in the Middle Ages, when copper became the predominant metal for coinage. Copper coins were cheaper and easier to produce than silver and gold coins, and they facilitated the expansion of trade and commerce. However, copper coins also had a lower intrinsic value than silver and gold coins, and they were subject to inflation and debasement. Today, copper is still used in some coins, such as the US 1-cent coins, but only as a minor component. The US 1-cent coins are composed of 2.5% copper and 97.5% zinc.[8]

III. Historical developments of the foreign exchange market

Foreign exchange trading, or forex trading, refers to the practice of buying and selling currencies in the global market with the intention of generating profits. This practice has a long history that dates back to the ancient times of Babylon, where merchants exchanged different types of coins and commodities. The modern forex market, however, is a result of several historical events that shaped the international monetary system, such as the Bretton Woods agreement and the gold standard. These events established the rules and institutions for the regulation and coordination of currency exchange rates, as well as the role of the US dollar as the dominant reserve currency. Today, the forex market is one of the largest, most liquid and

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[7] HDFC Bank. "What is Foreign Exchange?" Accessed from https://www.hdfcbank.com/personal/resources/learning-centre/pay/know-what-is-foreign-exchange.

[8] Tradeciety. "The History Of Currency Trading And The Forex Market." 19 July 2015. Accessed from https://tradeciety.com/the-history-of-currency-trading-and-the-forex-market.

accessible markets in the world, with an average daily turnover of more than $6 trillion. The forex market operates 24 hours a day, five days a week, and involves a network of banks, brokers, traders, investors and central banks from different countries and regions.[9] Certain systems of exchange are classified below:

1. **Barter system:** The barter system is an ancient method of exchange that originated in Mesopotamia around 6000BC. It involves trading goods and services without using money. Some commodities, such as salt and spices, became widely accepted as mediums of exchange. The barter system still exists today as a form of counter-trade. It offers various advantages to businesses, such as clearing excess inventory, utilizing idle resources, increasing sales, accessing new markets, providing interest-free credit, restructuring debt, facilitating foreign trade.[10]
2. **Gold coins exchange system:** The first gold coins, produced in the 6th century BC, functioned as currency due to their portability, durability, divisibility, uniformity, scarcity and acceptability. The earliest metal money, from 1000 B.C. China, consisted of stamped pieces of precious metals, such as bronze and copper. In 1816, England adopted the gold standard, which ensured the government's redemption of paper money for its gold value. The U.S. followed with the Gold Standard Act in 1900, which led to the establishment of the central bank that plays a vital role in the economy today. However, the gold standard could not withstand the world wars and collapsed in the 1930s due to the Depression and the devaluation of gold.[11]
3. **Bretton Woods System:** The Bretton Woods system was a post-war international monetary system established in 1944 at the United Nations Monetary and Financial Conference in Bretton Woods, New Hampshire, USA. The system established the U.S. dollar as the primary reserve currency, which was linked to gold at a predetermined rate and could be exchanged for the precious metal upon demand. This system aimed to promote stability and prevent competitive devaluations among countries. It also created the International Monetary Fund (IMF) and the World Bank to foster international monetary cooperation and provide financial assistance for reconstruction and development. The Bretton Woods system contributed to the post-war economic stability but collapsed in 1971 when President Richard

[9] Bradfield, David. "The History of Forex." 19 December 2018. Accessed from *DailyFX*, https://www.dailyfx.com/education/beginner/history-of-forex.html.

[10] Ozgul, U. Y. A. N. "Barter system as an innovative and alternative financial and trade model during the periods of economic crisis and recession and its importance for businesses." *PressAcademia Procedia* 4.1 (2019): 340-348.

[11] Mint.com. "The History of Money: How Our Currency Evolved from Pelts to Money." 7 August 2009, Accessed from https://mint.intuit.com/blog/investments/the-history-of-money/#entry-sources.

M. Nixon ended the U.S. dollar's convertibility to gold, leading to the free floating of the U.S. dollar against other foreign currencies.[12]

4. **The Free-Floating System:** The international monetary system transitioned from the Bretton Woods fixed exchange rate system to a more flexible exchange rate system known as the "free-floating" or "floating exchange rate" system during the 1970s and 1980s. Under this system, exchange rates were determined by supply and demand in the foreign exchange market, without any fixed peg to other currencies or gold. This system allowed currencies to adjust to economic conditions more freely but also introduced greater exchange rate volatility. This transition brought about significant changes in the way exchange rates were determined, as they were no longer fixed but instead fluctuated based on market forces. In the 1980s, there were notable shifts in exchange rate systems in various countries, particularly in response to economic and geopolitical factors. The collapse of the system led to the adoption of the floating exchange rate regime.[13]
5. **The Plaza Accord:** One of the significant events in the 1980s was the Plaza Accord. The U.S. dollar experienced a significant appreciation against the other major currencies in the early 1980s. In 1985, the finance ministers and central bank governors of the G5 countries (United States, Japan, Germany, France, and the United Kingdom) convened a secret meeting at the Plaza Hotel in New York City and agreed to devalue the U.S. dollar relative to the Japanese yen and the German mark. The Plaza Accord aimed to reduce the U.S. trade deficit by depreciating the U.S. dollar and marked a shift from a free-floating system to a more managed exchange rate system. The accord achieved its main objective of weakening the dollar but not all of its policy goals were met.[14]
6. **Rise of the Euro:** The Euro emerged as a result of several treaties that aimed to enhance the integration of the European countries after the Second World War. In 1992, a conference was held in the Dutch city of Maastricht and a treaty referred to as the Maastricht Treaty was signed. The treaty established the European Union (EU) and laid down the criteria for European Union member states to join the Economic and Monetary Union (EMU) and adopt the Euro as their currency. After a decade of preparation, the Euro was launched on January 1, 1999, with 12 European countries. Coins and banknotes were introduced on January 1,

[12] Eichengreen, Barry. Global imbalances and the lessons of Bretton Woods. Mit Press, 2010.
[13] Dornbusch, Rudiger, and Jeffrey Frankel. "The flexible exchange rate system: experience and alternatives." International Finance and Trade in a Polycentric World: Proceedings of a Conference held in Basel by the International Economic Association. London: Palgrave Macmillan UK, 1988.
[14] James Chen. "Plaza Accord: Definition, History, Purpose, and Its Replacement." July 25, 2021. Accessed from https://www.investopedia.com/terms/p/plaza-accord.asp#:~:text=1,such%20as%20implementing%20tax%20cuts.

2002, and the largest cash changeover in history took place from 12 former currencies. The EUR/USD currency pair constitutes the most liquid and widely traded pair among all currency pairs in the foreign exchange market.[15]

7. **Internet Trading:** Internet trading, also known as online trading or e-trading, emerged in the mid-1990s with the development and popularization of the World Wide Web.[16] During this time, the currency markets became more sophisticated and faster than ever, as the attitude of people towards using money changed. The spread of personal computers and the improvements in internet connectivity and security technology enabled online trading for a growing number of people. A person sitting alone at home could access, with the click of a button, an accurate price that only a few years prior would have required a team of traders, telephones and brokers. Internet trading rapidly expanded to include not only stocks but also other financial instruments like options, futures, and forex. Trading platforms became more advanced and user-friendly.

In terms of transactional volume, the foreign exchange market holds the distinction of being the most substantial globally today. The future of foreign exchange is full of uncertainty and change, creating endless opportunities for forex traders.

IV. Foreign exchange market segments

Forex market segments can be classified based on various factors. The following are some common segments of the forex market:

- **Spot Market:** The spot forex market trades currencies for immediate delivery and settlement, usually within two business days. It is the most prevalent segment of the forex market where participants exchange one currency for another at the prevailing market price. It involves buyers and sellers from across the entire spectrum of the financial sector.
- **Forward Market:** The forward forex market trades currency contracts for future delivery and settlement at a predetermined date and exchange rate. No actual exchange of currencies occurs, only the value. It allows participants to hedge against currency risk.
- **Futures Market:** The futures market is similar to the forward market, except that forex futures are standardized contracts traded on organized exchanges. These contracts

[15] Huzefa Hamid. "The History of Forex Trading." April 02, 2008. Accessed from https://www.dailyforex.com/forex-articles/2008/04/the-history-of-forex-trading/66.

[16] Bhasin, Madan Lal. "E-broking as a tool for marketing financial services in the global market." *Journal of services Research* 5.2 (2005): 151.

specify the currency pair, contract size, settlement date, and price. Forex futures can be used for speculation and hedging.[17]

- **Options Market:** The forex options market gives participants the right (but not the obligation) to buy or sell currencies at a specified price on or before a predetermined date. Forex options provide flexibility for managing risk.
- **Interbank Market:** The interbank forex market is a decentralized market where banks, financial institutions, and large corporations trade currencies directly with each other. It is the core of the forex market and sets benchmark exchange rates.
- **Retail Market:** Retail forex, also known as the over-the-counter (OTC) market, is where individual traders and small investors participate in forex trading through brokers. It offers access to the forex market for retail participants.
- **Electronic Communication Network (ECN):** ECNs are electronic trading platforms that connect various market participants, allowing for direct and transparent trading without the need for intermediaries. They provide access to better pricing and order execution.[18]
- **Cryptocurrency Exchange:** Some cryptocurrency exchanges offer trading pairs that involve cryptocurrencies and fiat currencies, essentially functioning as a subset of the forex market. These exchanges enable the trading of digital currencies like Bitcoin against traditional currencies.[19]

These are some of the key segments of the forex market, each catering to the specific needs and preferences of different participants, from large financial institutions to individual retail traders.

V. Analysis of the Regulatory Framework for Foreign Exchange Transactions in India

A. Foreign Exchange Regulation Act (FERA), 1973[20]

The Foreign Exchange Regulation Act (FERA), 1973 was a legislation enacted by the Indian Parliament to regulate and control foreign exchange transactions and certain aspects of overseas investments in India. The Act came into force in 1974 and remained in operation until 1991. The main objective of FERA was to conserve the scarce foreign exchange reserves of the

[17] Akhilesh Ganti. "Foreign Exchange Market: How It Works, History, and Pros and Cons." June 29, 2023. Accessed from https://www.investopedia.com/terms/forex/f/foreign-exchange-markets.asp

[18] Markham, Jerry W., and Daniel J. Harty. "For whom the bell tolls: the demise of exchange trading floors and the growth of ECNs." *J. Corp. L.* 33 (2007): 865.

[19] Davison, Claire, et al. "Evaluation of sustainable digital currency exchange platforms using analytic models." *Sustainability* 14.10 (2022): 5822.

[20] Act number 46 of 1973.

country and to prevent their misuse or diversion for unauthorized purposes.[21] FERA applied to all citizens of India, whether residing in India or abroad, and to all branches, offices and agencies outside India owned or controlled by a person resident in India. FERA was repealed on December 29, 1999, by the Foreign Exchange Management Act (FEMA), 1999, which marked a paradigm shift in the approach towards foreign exchange regulations in India.

FERA was introduced at a time when India faced a severe foreign exchange crisis and adopted a restrictive and regulated economic policy. The Act aimed to regulate and monitor all transactions involving foreign exchange, including dealings in foreign currency, securities and immovable property situated outside India.[22] FERA also provided a legal framework for regulating various aspects of foreign investments in India, such as approval, repatriation, transfer and acquisition of shares. FERA was based on the presumption that all foreign exchange earned by Indian residents rightfully belonged to the Government of India and had to be collected and surrendered to the Reserve Bank[23] of India (RBI). Therefore, FERA prohibited all transactions that were not expressly permitted by the RBI or the Central Government. FERA also contained provisions to curb smuggling and other illegal activities related to foreign exchange and to ensure the proper utilization of foreign exchange for the economic development of the country.

FERA was in force during a period when India followed a more inward-looking and protectionist economic policy. However, with the onset of economic liberalization and globalization in the 1990s, India adopted a more open and market-oriented approach to foreign exchange regulations. This led to the enactment of the Foreign Exchange Management Act (FEMA) in 1999, which replaced FERA as the governing legislation for foreign exchange transactions in India. FEMA aimed to facilitate external trade and payments and to promote the orderly development and maintenance of the foreign exchange market in India. FEMA applied to all persons resident in India and to all branches, offices and agencies outside India owned or controlled by a person resident in India. FEMA was based on the principle of management and regulation of foreign exchange, rather than control and restriction. Therefore, FEMA allowed all transactions that were not expressly prohibited or restricted by the RBI or the Central Government. FEMA also provided for the imposition of civil penalties for contravention of its provisions, rather than criminal prosecution as under FERA.

[21] Section 2(h) of Foreign Exchange Regulation Act, 1973.
[22] Section 2(g) of Foreign Exchange Regulation Act, 1973.
[23] Section 2(t) of Foreign Exchange Regulation Act, 1973.

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RBI's Power to Issue Directions to Authorized Person:

- The Reserve Bank may holds the power to authorize any person to be known as authorized person[24] to deal in foreign exchange or in foreign securities, as an authorized dealer, money changer[25] or off-shore banking unit. RBI has the power to inspect[26] any authorised authority and has the power to search suspected persons and to seize documents.
- The Reserve Bank may give any direction in regard to making of payment or the doing or desist from doing any act relating to foreign exchange or foreign security, to the authorized persons it can also direct any authorized person to furnish such information, in such manner, as it deems fit for the purpose of securing compliance with the provisions of this Act and of any rules and regulations.
- Where any authorized person contravenes any direction given by the Reserve Bank under this Act, the RBI may, after giving reasonable opportunity of being heard, impose on the authorized person a penalty which may extend to ten thousand rupees and in the case of continuing contravention with an additional penalty which may extend to two thousand rupees for every day during which such contravention continues.[27]
- In accordance with the regulations of the Reserve Bank of India (RBI), foreign nationals seeking to practice a profession within the country are required to obtain prior authorization. The RBI retains the authority to request information, including but not limited to, details pertaining to Indian currency, foreign exchange transactions, and accounting records from any individual as deemed necessary. This is in line with the RBI's mandate to maintain the country's financial stability and integrity.

FERA had several shortcomings. Some of them included complex regulatory procedures, bureaucratic hurdles, and restrictions that hindered foreign exchange transactions. Additionally, the act was criticized for being too rigid, creating a challenging environment for businesses and investors. The law violators were treated as criminal offenders under this Act. Wide number of powers was given in the hand of Enforcement Directorate to arrest any person and seize any document. It was seen as a hindrance to economic liberalization and was eventually replaced to address these shortcomings.

In response to the evolving economic landscape of India, the Government of India drafted the

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[24] Section 10 of Foreign Exchange Regulation Act, 1973.
[25] Section 2(m) of Foreign Exchange Regulation Act, 1973.
[26] Section 12 of Foreign Exchange Regulation Act, 1973.
[27] Section 11 of Foreign Exchange Regulation Act, 1973.

Foreign Exchange Management Bill (FEMA) as a replacement for the Foreign Exchange Regulation Act (FERA). This legislative change was necessitated by the increasing misalignment of FERA with the government's liberalization objectives. The introduction of FEMA represents a significant shift in the regulatory framework governing foreign exchange in India, reflecting the country's transition towards a more open and globally integrated economy. Foreign Exchange Management Act (FEMA) in 1999, reflects a more liberalized approach to foreign exchange regulation in India. It helps for creating a new foreign exchange management program that adhered to the World Trade Organization's evolving framework (WTO). Notwithstanding the drafting of the Foreign Exchange Management Bill (FEMA), the provisions of the Foreign Exchange Regulation Act (FERA) remained in force until the formal enactment of FEMA. This interim period ensured the continuity of regulatory oversight over foreign exchange activities in India.

B. Foreign Exchange Management Act (FEMA), 1999[28]

The Foreign Exchange Management Act (FEMA) is an Indian legislation enacted in 1999 by the Indian Parliament with the objective of "consolidating and amending the laws relating to foreign exchange to facilitate external trade and payments and to promote the orderly development and maintenance of the foreign exchange market in India." It replaced the Foreign Exchange Regulation Act (FERA) and aimed to liberalize and simplify foreign exchange controls in India. The Reserve Bank of India (RBI)[29] administers FEMA and regulates foreign exchange transactions and facilitates external trade and payments. FEMA is a regulatory framework that empowers the RBI and the Central Government to issue rules and regulations on foreign exchange in accordance with India's Foreign Trade Policy. The Enforcement Directorate[30], headed by the Director, is the Head Office of FEMA located in New Delhi. It has five zonal offices in Delhi, Mumbai, Kolkata, Chennai, and Jalandhar, each headed by a Deputy Director. These five zones are further divided into seven sub-zonal offices headed by Assistant Directors and five field units headed by Chief Enforcement Officers.

The Foreign Exchange Management Act (FEMA) establishes a clear distinction between transactions related to the current account and those pertaining to the capital account. It reflects India's move toward a more liberalized and market-oriented economy, reducing restrictions on foreign exchange transactions. It authorizes the Central Government to regulate the flow of payments to and from a person resident outside India. The act empowers the RBI to authorize

[28] Act number 42 of 1999.
[29] Section 11 of Foreign Exchange Management Act, 1999.
[30] Section 36 Foreign Exchange Management Act, 1999.

certain persons or entities to deal in foreign exchange, subject to specified conditions. The Government of India can impose restrictions on an authorized person from undertaking foreign exchange transactions on the current account, in the public interest. FEMA includes provisions for the enforcement of its regulations and imposes penalties for violations, aiming to ensure compliance with foreign exchange laws. Offences involving foreign exchange are now considered civil offences under this act. It extends to the whole of India. Adjudicating authorities[31] and an Appellate Tribunal[32] are established under FEMA to address disputes and appeals related to foreign exchange violations.

Penalties: A person who contravenes any provision of FEMA or any rule, direction, regulation, order or notification issued under FEMA, is liable to pay a penalty up to three times the amount involved in such contravention or up to Rs.2 lakh. In case of a continuing contravention, a further penalty which may extend to Rs.5,000 for every day during which the contravention continues, is also imposed. [33] A person who acquires any foreign exchange, foreign security or immovable property, situated outside India, of the aggregate value exceeding the threshold prescribed u/s. 37A (at present no limit has been prescribed), is liable to penalty up to three times the amount involved, confiscation of the value equivalent situated in India, and imprisonment for a term that may be subject to an extension of up to five years, accompanied by a monetary penalty. The competent authorities may also confiscate any currency, security or property in addition to imposing penalty. If the person fails to pay the penalty within 90 days, he is liable for civil imprisonment.

C. Difference Between FERA and FEMA

1. Foreign Exchange Regulation Act (FERA) was passed by the parliament in 1973. It came into force from January 1, 1974 while Foreign Exchange Management Act (FEMA) was passed by parliament on 2 December 1990 and came into force from June 2000.
2. FERA was repealed by Vajpayee Govt. in 1998 while FEMA succeeded FERA. FERA consists of 81 Sections and was more complex while FEMA consists of 49 Sections and has no more provisions.
3. FERA considered foreign exchange as a scarce resource while the other considers foreign exchange as an asset. Presumption of mens rea and joining hands in offences

[31] Section 2(a) of Foreign Exchange Management Act, 1999.
[32] Section 2(b) of Foreign Exchange Management Act, 1999.
[33] Section 13 of Foreign Exchange Management Act, 1999.

existed in FERA, while these were not there in FEMA.

4. Violation of rules under the former Act was considered as criminal offence and the accused was not provided with any legal assistance. Violation of rules under the later is considered as civil offence and the accused is provided with the legal assistance.
5. Terms like Capital Account Transaction, current Account Transaction, person, service etc. were not defined in FERA. These terms have been defined in detail in FEMA. Definition of Authorized Person[34] has been widened under FEMA but in former Act it was very narrow in scope.
6. The objective of FERA was conservation of foreign exchange & it regulated the foreign payments. The objective of FEMA is Management of foreign exchange and it focused on increasing the foreign exchange reserves & foreign trade of India.
7. Under this Act there were no provisions for tribunal and the appeals were laid to High Court only, while there are provisions of special director[35] and special tribunal under this later Act.
8. Prior approval of RBI was required for transferring funds for external affairs under FERA but there's no need of prior approval from RBI under FEMA.
9. The monetary punishment under the former Act was approximately five times to that of amount involved while under FEMA, it is reduced to three times to that of amount involved.

In spite of the differences, there are some similarities between FERA and FEMA also that the Reserve Bank of India and central government would continue to be the regulatory bodies, presumption of extra territorial jurisdiction as envisaged in FERA has been retained, and the directorate of enforcement continues to be the agency for enforcement of the provisions of the law such as conducting search and seizure.[36] Thus the Foreign Exchange Regulation Act governed everything related to foreign exchange. Even though it was enacted with the greatest Intentions, the unnecessarily rigorous limitations it imposed hampered the expansion of Indian Industries and forex market. However, with the implementation of FEMA, the situation quickly shifted from control to management, allowing for the development and orderly regulation of India's foreign exchange market and the overall development of Indian economy.

Ultimately both, the Foreign Exchange Regulation Act (FERA) and the Foreign Exchange

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[34] Section 2(c) of Foreign Exchange Management Act, 1999.
[35] Section 2(zc) of Foreign Exchange Management Act, 1999.
[36] Section 37 of Foreign Exchange Management Act, 1999.

Management Act (FEMA) both played crucial roles in shaping India's economic policies. FERA was later replaced by FEMA in 1999, which provided greater flexibility and liberalization. The Acts allowed for increased foreign direct investment by providing a conducive environment for foreign companies to invest in India, leading to capital inflows and job creation. The Acts facilitated India's integration into the global economy, allowing for participation in international trade and benefiting from globalization trends. It's important to note that while these acts brought about several positive changes, they also posed challenges and required continuous monitoring to prevent misuse and ensure the stability of the Indian economy.

VI. Emergence of smuggling activities

Smuggling is the illegal transportation, import, or export of goods or items across borders or within a country, typically in violation of customs, trade, or taxation laws.[37] Smugglers engage in these activities to avoid paying duties, taxes, or other legal restrictions imposed by governments. The items being smuggled can vary widely and may include goods like contraband, narcotics, weapons, wildlife, or even people. Smuggling often involves secrecy, evasion of law enforcement, and sometimes dangerous or covert methods to move goods or individuals across borders or regions without detection by authorities. Smuggling is illegal and is generally seen as a criminal activity in most countries. Penalties for smuggling can be severe, including fines, imprisonment, and other legal consequences. [38]

(A) Smuggling Activities in India

Smuggling activities in India have a long history, dating back centuries. Smuggling typically involves the illegal transportation of goods, often to avoid taxes or import/export restrictions. India has been a center of trade for centuries, with ancient trade routes like the Silk Road passing through the region. These routes facilitated the exchange of goods, and smuggling could have arisen as a means to avoid taxes or tariffs imposed by various rulers and empires. Smuggling likely occurred during various periods of ancient Indian history, including the Indus Valley Civilization (circa 2600-1900 BCE) and the Vedic period (circa 1500-500 BCE). These activities might have involved the movement of valuable goods like spices, textiles, and metals. During the reign of Emperor Ashoka and the Mauryan Empire[39], there were efforts to regulate

[37] Kulish, Anatolii Mykolaiovych, et al. "Smuggling as a threat to economic security of the state." (2021).
[38] Karras, Alan L. "Smuggling: Contraband and corruption in world history." Rowman & Littlefield Publishers, 2009.
[39] Mishra, S. C. "A Landmark Study of Mauryan India." *Social Scientist*, vol. 33, no. 11/12, 2005, pp. 76–92. JSTOR, Accessed from http://www.jstor.org/stable/3518067.

trade and impose taxes on goods. This may have led to smuggling activities as traders sought to avoid such levies. After that the Gupta Empire[40] was known for its prosperous trade, and the movement of goods, both legally and illegally, likely played a role in the economic life of the empire.

India was a major center for trade during the medieval period. Smuggling may have been prevalent in response to various regional rulers and their trade policies. The Mughal Empire(16th to 18th century), with its vast and prosperous domains, implemented regulations and taxes on trade, smuggling became common during this period, as merchants sought to evade these taxes, especially on valuable commodities like spices, textiles, and gems. Throughout Indian history, various regional empires and kingdoms ruled different parts of the subcontinent, each with its trade policies and taxes. Smuggling activities likely persisted in response to these local regulations. Smuggling in pre-British India was a complex and dynamic phenomenon influenced by factors such as economic conditions, trade routes, and the policies of ruling authorities. The British East India Company was granted a royal charter in 1600[41], and it established trading posts in India. Initially, the company focused on the export of Indian textiles to Europe, but as their presence grew, they imposed tariffs and trade restrictions, which led to increased smuggling. Smuggling activities gained momentum between 17th to 18th century, particularly in response to the Company's oppressive trade practices. Indian textiles, opium, and other valuable commodities were smuggled out of India, while European goods were smuggled into the country. In the nineteenth century, British India witnessed the illicit trade of salt across its provincial borders, which were subject to varying rates of taxation. Similarly, the movement of goods liable to duty between Goa and India, and between Gibraltar and Spain, also constituted smuggling activities. From early to Mid-20th Century, the Indian independence movement gained momentum, smuggling became linked with the political and economic struggle for freedom. The Quit India Movement in 1942[42], for example, included boycotts and smuggling activities as acts of resistance against British rule. Overall, smuggling activities in India during the British Empire were influenced by the economic policies, trade regulations, and political climate of the time. Smuggling served as a means of economic survival, resistance, and circumventing colonial oppression during this extensive period of colonial rule.

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[40] Goyal, Shankar. "Historiography Of The Imperial Guptas: Old And New." *Annals of the Bhandarkar Oriental Research Institute*, vol. 77, no. ¼, 1996, pp. 1–33. JSTOR, Accessed from http://www.jstor.org/stable/41702162.
[41] Evans, Frank. "The Evolution of the English Joint Stock Limited Trading Company." *Columbia Law Review*, vol. 8, no. 5, 1908, pp. 342. JSTOR, Accessed from https://doi.org/10.2307/1110068.
[42] Chakrabarty, Bidyut. "Political Mobilization in the Localities: The 1942 Quit India Movement in Midnapur." *Modern Asian Studies*, vol. 26, no. 4, 1992, pp. 791–814. JSTOR, Accessed from http://www.jstor.org/stable/312940.

After gaining independence in 1947, India continued to grapple with smuggling issues, including the illegal trade of goods, narcotics, and other contraband. The country established stricter customs regulations and law enforcement agencies to address these challenges. Excessive taxes and duties on certain goods, both during colonial rule and post-independence, have encouraged smuggling as a way to evade these financial burdens. India's extensive coastline, porous borders, and proximity to neighboring countries make it vulnerable to smuggling activities. The easy accessibility of routes for illicit trade, such as through land borders, sea routes, and even air transport, has contributed to the persistence of smuggling. The demand for goods that are banned, restricted, or heavily taxed, such as alcohol, narcotics, and certain luxury items, has created a market for smugglers to exploit. Corruption within law enforcement agencies and ineffective border controls has enabled smuggling to thrive. Smugglers often pay bribes to avoid detection or prosecution. Economic disparities and poverty in certain regions of India have led some individuals to engage in smuggling as a means of livelihood. Smuggling activities continue to be a challenge in India, and efforts to combat them involve a combination of law enforcement, border security, policy reforms, and international cooperation.

VII. Conclusion and suggestions

In summary, we can say that Forex enables international trade by providing a mechanism to exchange one country's currency for another. It is crucial for importing and exporting goods and services, as transactions often involve currencies from different countries. Exchange rates, which determine the value of one currency in terms of another, have a direct impact on a country's international competitiveness. A weaker domestic currency can make exports more attractive, while a stronger currency can make imports cheaper. A stable foreign exchange market is essential for economic stability. Sudden and drastic fluctuations in exchange rates can disrupt trade, investment, and economic growth. Central banks often intervene to maintain stability. Investors look at exchange rates when considering foreign investments. A favorable exchange rate can attract foreign capital, stimulating economic growth and infrastructure development. A country's exchange rate also affects its tourism industry. Exchange rates are considered when setting monetary policy. Central banks use interest rates and other tools to influence exchange rates, which, in turn, affect inflation, employment, and overall economic conditions. Some countries hold foreign currencies as part of their foreign exchange reserves. The U.S. dollar is a primary reserve currency, and its value can impact global economic stability. Forex markets provide tools for businesses to hedge against currency risk. This is essential for companies with international operations to protect against adverse currency

movements. Governments can generate revenue through foreign exchange, particularly through fees and taxes on currency transactions. Forex transactions are recorded in a country's balance of payments, which tracks the flow of money in and out of the country. A surplus or deficit in the balance of payments can affect a nation's economic health. Thus, foreign exchange is a critical component of a country's economic framework, impacting trade, investment, monetary policy, and overall economic stability. However illegal trafficking and smuggling activities also increases due to irregular and unbalanced foreign exchange. These activities have significant effects on a country's foreign exchange situation. In the context of India, smuggling primarily affects the forex by draining foreign exchange reserves. Moreover it leads to a significant outflow of foreign exchange because illicit goods are often traded for foreign currencies. This can deplete a country's foreign exchange reserves, making it harder to pay for essential imports. Smuggling activities can distort a country's balance of payments, as they are not recorded in official trade data. This can lead to inaccurate economic assessments and affect exchange rate policies. Smuggled goods often evade import duties and taxes, resulting in a loss of government revenue. This can impact fiscal policies and reduce resources available for public spending. To control and prevent smuggling and its impact on forex, India has implemented various measures. India has invested in improving customs enforcement by modernizing customs procedures, increasing personnel, and enhancing surveillance at ports, borders, and other entry points. Technology like electronic data interchange (EDI), scanning devices, and automated clearance systems have been adopted to enhance monitoring and reduce the scope for corruption. Intelligence-sharing and coordination among different law enforcement agencies, including customs, police, and paramilitary forces, have been improved to track and apprehend smugglers effectively. India has stringent anti-smuggling laws in place to deter smugglers and impose severe penalties on them. Efforts to raise public awareness about the negative consequences of smuggling have been made to discourage participation in illicit trade. India cooperates with other countries to address transnational smuggling, especially in cases where goods across international borders smuggled. Simplifying and rationalizing trade policies and reducing tariff rates on certain goods can reduce the economic incentives for smuggling. Efforts to promote legal trade and improve the ease of doing business can also help in reducing the attractiveness of smuggling. It's important to note that despite these measures, smuggling continued to some extent, driven by the high demand for certain goods and the economic incentives for smugglers. Smuggling in present days is a complex issue with social, economic, and political dimensions. Smuggling remains a challenge, and its complete eradication is difficult. The dynamic nature of smuggling activities and the vastness of India's borders and

coastline make it an ongoing concern. Nevertheless, the government continues to adapt its strategies to control and prevent smuggling and its adverse impact on the foreign exchange and the broader economy.

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