14

STANDING COMMITTEE ON PETROLEUM & NATURAL GAS (2011-12)

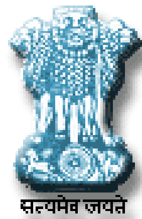
FIFTEENTH LOK SABHA

MINISTRY OF PETROLEUM & NATURAL GAS

CHALLENGES OF UNDER-RECOVERIES OF PETROLEUM PRODUCTS

[Action Taken by the Government on the recommendations contained in the Ninth Report (Fifteenth Lok Sabha) of the Standing Committee on Petroleum and Natural Gas (2011-12)]

FOURTEENTH REPORT



LOK SABHA SECRETARIAT
NEW DELHI

August, 2012/ Bhadrapada,1934 (Saka)

STANDING COMMITTEE ON
PETROLEUM & NATURAL GAS
(2011-12)

FIFTEENTH LOK SABHA

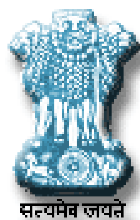
MINISTRY OF PETROLEUM & NATURAL GAS

CHALLENGES OF UNDER-RECOVERIES OF PETROLEUM PRODUCTS

[Action Taken by the Government on the recommendations contained in the Ninth Report (Fifteenth Lok Sabha) of the Standing Committee on Petroleum and Natural Gas (2011-12)]

Presented to Lok Sabha on 30.8.2012

Laid in Rajya Sabha on 30.8.2012



LOK SABHA SECRETARIAT
NEW DELHI

August, 2012/ Bhadrapada,1934 (Saka)

Contents

		Page
COMPOSITION OF THE COMMITTEE (2011-12)………………………		**(iii)**
INTRODUCTION …………………………………………………………		**(iv)**
CHAPTER I	Report ………………………………………………….	
CHAPTER II	Recommendations/Observations which have been accepted by the Government ……………………………	
CHAPTER III	Recommendations/Observations which the Committee do not desire to pursue in view of the Government's replies …………………………………	
CHAPTER IV	Recommendations/Observations in respect of which replies of the Government have not been accepted by the Committee ……………………………………	
CHAPTER V	Recommendations/ Observations in respect of which final replies of the Government are still awaited ……	

ANNEXURES

I.	Minutes of the Fourth sitting of the Standing Committee on Petroleum and Natural Gas (2011-12) held on 27.08.2012	
II.	Analysis of the Action Taken by the Government on the Recommendations contained in the Ninth Report (Fifteenth Lok Sabha) of the Standing Committee on Petroleum and Natural Gas (2011-12) on `Challenges of Under-recoveries of Petroleum Products'	

COMPOSITION OF THE STANDING COMMITTEE ON PETROLEUM & NATURAL GAS
(2011-12)

Shri Aruna Kumar Vundavalli - Chairman

Lok Sabha

2 Shri Vikrambhai Arjanbhai Madam Ahir
3 Shri Badruddin Ajmal
4 Shri Ramesh Bais
5 Shri Sudarshan Bhagat
6 Shri Sanjay Singh Chauhan
7 Smt. Santosh Chowdhary
8 Shri Raosaheb Dadarao Danve
9 Shri Kalikesh N. Singh Deo
10 Shri Mukeshkumar Bheravdanji Gadhvi
11 Shri Dilipkumar Mansukhlal Gandhi
12 Dr. Thokchom Meinya
13 Shri Mahabal Mishra
14 Shri Kabindra Purkayastha
15 Shri M.B. Rajesh
16 Shri C.L. Ruala
17 Shri Brijbhushan Sharan Singh
18 Shri Dhananjay Singh
19 Shri Uday Pratap Singh
20 Shri C. Sivasami
21 Shri Thol Thirumaavalavan

Rajya Sabha

22 Dr. Akhilesh Das Gupta
23 Shri Ahmed Patel
24 Smt. Gundu Sudharani
25 Dr. Prabha Thakur
26 Prof. Ram Gopal Yadav
27 Shri Sabir Ali
28 Shri Pankaj Bora
29 Shri Tapan Kumar Sen
30 Shri Shankarbhai N. Vegad
31 Shri Mansukh L. Mandaviya

Secretariat

1. Shri A.K.Singh - Joint Secretary
2. Smt. Anita Jain - Director
3. Shri H.Ram Prakash - Deputy Secretary

INTRODUCTION

I, the Chairman, Standing Committee on Petroleum & Natural Gas having been authorised by the Committee to submit the Report on their behalf, present this Fourteenth Report on Action Taken by the Government on the recommendations contained in the Ninth Report (Fifteenth Lok Sabha) of the Committee on 'Challenges of Under-recoveries of Petroleum Products'.

2. The Ninth Report of the Standing Committee on Petroleum & Natural Gas was presented to Lok Sabha on 22 December, 2011. The Action Taken Replies of the Government to all the recommendations contained in the Ninth Report were received on 23 March, 2012.

3. The Standing Committee on Petroleum & Natural Gas (2011-12) considered and adopted the Report at their sitting held on 27 August, 2012.

4. An analysis of the action taken by the Government on the recommendations contained in the Ninth Report (Fifteenth Lok Sabha) of the Standing Committee on Petroleum & Natural Gas is given in Annexure-II.

5. The Committee place on record their appreciation for the valuable assistance rendered to them by the officers of the Lok Sabha Secretariat attached to the Committee.

New Delhi;
27 August, 2012
5 Bhadrapada,1934 (Saka)

ARUNA KUMAR VUNDAVALLI,
Chairman,
Standing Committee on
Petroleum & Natural Gas.

CHAPTER I

REPORT

This Report of the Standing Committee on Petroleum & Natural Gas deals with the action taken by the Government on the Recommendations contained in the Ninth Report (Fifteenth Lok Sabha) of the Standing Committee on Petroleum and Natural Gas (2011-2012) on 'Challenges of Under-recoveries of Petroleum Products', which was presented to Lok Sabha on 22.12.2011.

2. Action Taken Notes have been received from the Government in respect of all the 17 Recommendations /Observations contained in the Report. These have been categorized as follows:-

(i) Recommendations/Observations that have been accepted by the Government:- SI.Nos. 1, 5, 7, 10, 12, 13 ,15 and 17.

(Chapter- II)

(ii) Recommendations/Observations which the Committee do not desire to pursue in view of the Government's replies SI. Nos.- 16 .

(Chapter-III)

(iii) Recommendations/Observations in respect of which replies of the Government have not been accepted by the Committee:- SI.No. 2, 3, 8 and 14.

(Chapter-IV)

(iv) Recommendations/Observations in respect of which final replies of the Government are still awaited : - SI. Nos. 4 ,6, 9 and 11 .

(Chapter-V)

3. The Committee desire that the Action Taken Notes on the Recommendations/Observations contained in Chapter-I of this Report and Final Replies in respect of the recommendations for which interim replies have been furnished by the Government (included in Chapter-V), should be furnished expeditiously.

4. The Committee will now deal with the action taken by the Government on some of their recommendations.

A. Refinery Gate Price-APM prices Vs. TPP/IPP.

Recommendation (Sl. No. 2, Para No. 2.2)

5. The Committee noted that during 1976-2002, pricing of sensitive petroleum products was based on Administrative Pricing Mechanism (APM). Under APM, cost of Crude oil processed by Refineries was fixed taking into account the delivered cost of crude oil and the normative refining cost. Further, besides normative marketing and distribution costs, Oil Marketing Companies (OMCs) were also allowed 12% post-tax returns. The Committee had been informed that the APM was reported to be increasingly unsuitable for the long term growth and efficiency of oil industry due to lack of adequate financial resource generation and incentives for investment in technological upgradations or cost minimization and for achieving consumer friendly and competitive vibrant petroleum sector. As such APM was fully dismantled with effect from 1st April 2002 and since then refinery gate prices of four sensitive petroleum products viz. petrol, diesel, LPG and kerosene are being governed by IPP/TPP which includes beside FOB price of petroleum products in the Arab Gulf, other components namely ocean freight, custom duty, insurance charges etc. in case of IPP and advance licensing benefits in case of EPP.

While going into merits of cost plus mechanism and TPP/IPP mechanism, the Committee were informed that actual cost of refinery/production of individual product was not identifiable separately due to operational procedures and TPP/IPP mechanism based on widely traded and international market price reflect the competitive conditions and help refineries to optimize turnover and over and above cost. The Committee while accepting the contentions of the Ministry for going in TPP/IPP mechanism were, however, of the view that when the refinery gate prices has been aligned to international market prices there is no justification of including other costs in TPP/IPP on the reasons that these costs have been incurred by refineries while importing crude oil.

Moreover the value of these components is less than 2% of the finished product cost and the refineries will not be much affected on exclusion of these components from the refinery gate prices.

The Committee, therefore, strongly recommended that the components other than FOB price of petroleum products at Arab Gulf should not be included in the refinery gate price which will bring down the cost of petroleum products and consequently reduce the under recoveries of OMCs.

6. In response, the Ministry of Petroleum & Natural Gas has submitted as below:-

"As per the current pricing mechanism, the Refinery Gate Price (RGP) of Petrol and Diesel is determined based on Trade Parity Price (as per the recommendations of Rangarajan Committee Report) whereas the RGP of PDS Kerosene and Domestic LPG is determined based on Import Parity Price. Based on the RGP effective 16th January 2012 for Petrol and Diesel and 1st January 2012 for PDS Kerosene and Domestic LPG, the impact of elements of customs duty, ocean freight, insurance charges, ocean loss, LC Charges and port dues etc. included in RGPs at Mumbai is given below

(Rs. / KL)

	Petrol	**Diesel**	**PDS Kerosene**	**Domestic LPG**
Elements included in	1,097	1,219	222	306
RGP	39,710	44,633	40,641	43,819
%	2.76%	2.73%	0.55%	0.70%

As may be seen from the above table, with the gradual reduction in the customs duty on crude and POL products, the current impact of elements (other than FOB) in the RGP is only around 0.5% to 2.8%. This ensures that refineries recover their cost of imports of raw material and also various other levies i.e. octroi, entry tax etc. on the refineries.

Hence RGP based on FOB would not cover the cost of refining crude oil particularly by the existing older refineries of PSU OMCs and would not be adequate to meet their CAPEX requirements towards capacity addition, quality up-gradation, etc.

In view of the above, it is not advisable to fix the RGP of petroleum products at FOB price".

7. As the Government have moved away from the cost plus regime and the Refinery Gate Price of petroleum products have been aligned to international market prices, the Committee had found no justification in including the components other than FOB price of petroleum products at Arab Gulf on the reasons that these costs have been incurred by refineries while importing crude oil.

The Ministry in its action taken reply have stated that the current impact of components other than FOB price in the RGP is only 0.5% to 2.8% which ensures that refineries recover their cost of imports and various other levies such as octroi , entry tax etc. Hence RGP based on FOB would not cover the cost of refining crude oil particularly by the older refineries of PSU OMCs and would not be adequate to meet their CAPEX requirements towards capacity addition, Quality up-gradation, etc.

The Committee are not satisfied with the action taken reply of the Ministry. The switch over from cost-plus mechanism to TPP-IPP mechanism was to reflect

the competitive conditions and help refineries to optimize turnover and bring efficiency in their operations. The Committee are of the opinion that by adding other costs to FOB which are notional, will defeat this objective besides inflating the refinery gate price. The Committee, therefore, reiterate its earlier recommendation to exclude components other than FOB from refinery gate price which will bring down the cost of petroleum products and reduce the under-recoveries of OMCs.

B. Operating efficiencies of refineries.

Recommendation (Sl. No. 3, Para No. 2.3)

8. The Committee noted that the petroleum products prices in the international market do not always move in tandem with the crude oil prices but depend on the demand and supply constraints, seasonal fluctuations etc. The Committee had also been informed that out of 9 to 10 products that are produced from crude oil, three products are priced above crude oil prices and rest are traded below the crude prices. Moreover, there is around 10% fuel loss in processing of crude oil which increases the cost price of the finished products.

On consideration of the material submitted and deposition by representatives, the Committee were convinced that in current international marketing scenario where there are narrow margins, the Indian refineries have to be very efficient in order to compete and be viable and profitable. The Committee, however, found that the public sector refineries are mostly of small capacity and suffer from inherent disadvantages like locational disadvantages, old technologies which has adversely affected the GRM of the refineries.

The Committee were further informed that BPCL, Mumbai are paying 3% octroi to BMC for bringing crude oil to refinery. So far Rs.1140 crore are being paid annually on this account which has denied the profitability of the company.

The Committee recommended that expert group be constituted to evaluate the performance of each refinery taking into account various constraints faced by them and take effective steps to make them more efficient, viable and profitable.

9. In response, the Ministry of Petroleum & Natural Gas has submitted as below:-

"The Recommendation of the Committee has been noted for necessary action".

10. The Committee had observed that in the current international market scenario where there are narrow margins , the Indian refineries have to be very efficient in order to compete and be viable and profitable. The Committee had further observed that the public sector refineries are mostly of small capacity and suffer from factors like locational disadvantages, old technologies which has adversely affected the GRM of the refineries. The Committee, therefore , had recommended that an expert group should be constituted to evaluate the performance of each refinery taking into account the constraints faced by them and to take effective steps to make them more efficient and profitable.

The Ministry in this regard has stated that recommendations of the Committee have been noted for necessary action. However, The Committee have not been informed of the action taken in this regard as no details regarding the steps taken by the Ministry has been spelt out.

While expressing their displeasure at the casual reply of the Government, the Committee would like to reiterate its earlier recommendation and desire the Ministry to constitute an expert group at the earliest to study various constraints faced by each refinery and take steps to make them more effecient.

C. <u>Transportation through VLCC</u>

Recommendation (Sl. No. 4, Para No. 2.4)

11. The Committee noted with concern that although shipping strategy of oil companies has always been to maximize transportation of imported crude oil in Very Large Crude Carriers (VLCC) there are infrastructure constraints like draft restrictions and port jetty limitations at Mumbai port which do not allow VLCCs to berth in Mumbai. Hence, refineries in Mumbai are constrained to import crude oil through smaller size of vessels. The Committee had also been informed that at Visakhapatnam, the Single Point Mooring (SPM) system, which is going to start soon will enable receipt of crude oil through VLCC's. Considering the facts that Very Large Crude Carriers (VLCC), a widely used crude oil carrier that can carry about 270 TMT of crude oil and will be more economical in regard to volume of transporting imported crude, the Committee felt that infrastructure constraints like draft restrictions and port jetty limitations at Mumbai Port should have been addressed on urgent basis. The Committee, urged the Ministry to take up the matter with the appropriate

authorities to ensure that the required infrastructure to handle VLCC be built at all the ports off-loading crude oil at the earliest.

12. The Ministry of Petroleum & Natural Gas has submitted the following reply in this regard:-

> "Upgrading infrastructure facilities for imports is a continuous process and is being pursued keenly by all stakeholders. Presently,following actions have been taken/ are being taken in this regard:
>
> (i) Single Point Mooring (SPM) facility at Visakhapatnam Refinery of HPCL has been commissioned in February, 2011.
>
> (ii) SPM facility off Mangalore Coast and other auxiliary facilities including Buoy, Sub-sea pipeline, Booster pumping station and pipelines to refinery from the Strategic Storage facility is under construction at Mangalore and from booster pumping station to MRPL Coastal terminal, the mechanical completion shall be achieved by the end of 2012.
>
> (iii) Integrated Offshore Crude handling facilities project at Paradeep shall be completed by the end of 2012, ahead to completion of Paradeep Refinery.
>
> (iv) Crude Oil import infrastructure at West Coast by IOCL is under review".

13. The Committee had noted with concern, the infrastructural constraints faced by OMCs in maximizing the transportation of imported crude oil in very large crude carriers (VLCC) in Mumbai and had urged the Ministry to take up the matter with the appropriate authorities to ensure that the required infrastructure to handle VLCC be built at all the ports off-loading crude oil, at the earliest.

The Ministry, in its reply have informed the status of upgrading infrastructure facilities at Visakhapatnam and Mangalore coast. In regard to the constraints at the Mumbai port, the Ministry have stated that the crude oil import infrastructure at the West Coast by IOCL is under review.

The Committee feel that there in an urgent need to address the infrastructural constraints like draft restrictions and port jetty limitations at Mumbai port as the port handles crude oil imports to some major refineries. Therefore, the Committee desire that the aforesaid review of West Coast by IOCL be expedited and urgent steps be taken to upgrade infrastructural facilities at the Mumbai Port.

D. Custom duty on Petroleum Product

Recommendation (Sl. No. 8, Para No. 2.8)

14. The custom duty levied on the petroleum products which was 7.5% and subsequently revised to 2.5% in June, 2011 does not actually add to the revenues of the Government as product imports are almost nil owing to surplus refining capacity in the Country. Instead, the Committee understood that it goes in to the calculation of fixing the import parity prices of these products at international level which in turn increases consumer price. The Committee, therefore, recommended that the custom duties on petroleum products especially that on petrol and diesel be brought down to Nil from the present level of 2.5% to make it at par with the custom duty on crude oil which at present is Nil leaving no room for calculation of Refinery Gate price which is the average of 80% of Import Parity Price (IPP) and 20% of Export Parity Price (EPP). The Committee asked to be apprised in cost reduction of petroleum products at refinery level after recent decision of the Government to remove the entire custom duty on crude oil and how this would help in bringing down the refinery gate price.

15. In response, the Ministry of Petroleum & Natural Gas has submitted as below:-

"The effective rate of protection on Petrol and Diesel has come down from 10% in 2002 to 2.5% currently. In fact, the Customs Duty on other major petroleum products namely PDS Kerosene, Domestic LPG and ATF is NIL.Thus, the remaining small effective rate of protection available is essential to provide some level of protection to refineries most of which are in operation for a long period.

The refineries also incur irrecoverable taxes imposed by various State Governments which are offset by the effective rate of protection to ensure viability in refinery operations.

As regards the impact of recent reduction in Customs Duty on crude oil and petroleum products in June 2011 on Refinery gate price of the Petroleum products, the reduction in Refinery Gate Price is Rs.1.75 per litre on Petrol and Rs.1.87 per litre on Diesel at Mumbai.

Further, reduction in Customs Duty on crude oil and petroleum products in June 2011 has adversely affected the profitability of four North East refineries. This is due to the fact that the North East refineries do not process imported crude oil. Therefore, crude procurement cost for the North East refineries does not reduce corresponding to reduction in Customs Duty on crude oil. On the other hand, reduction in Customs Duty on products has brought down the Refinery Gate Prices leading to lesser sales realization. Hence any further reduction in Customs Duty on petroleum products, especially petrol and diesel would further worsen the deteriorating financial situation of the North East refineries that had arisen after duty restructuring in June, 2011.

It is also added that a 2.5% differential between basic Customs Duty on crude oil and petroleum products, is based on the recommendation of the Rangarajan Committee on pricing and Taxation of Petroleum, to provide a viable margin to domestic refineries".

16. As custom duty levied on petroleum products does not add to the revenues of the Government and only increase the refinery gate price of the petroleum products, the Committee had recommended that custom duties on petroleum products especially on petroleum and diesel be brought down to Nil from present level of 2.5%.

The Ministry in its reply had stated that the 2.5% custom duty is essential to provide some level of protection to refineries which are in operation for a long period. It has also stated that the refineries also incur irrecoverable taxes imposed by various State Governments which are offset by the effective rate of protection to ensure viability in sitting operations. The Ministry have further stated that reduction in custom duty would worsen the deteriorating financial position of the North-East refineries.

The Committee are however, not convinced by the reply of the Ministry. Though some refineries particularly in the North-East are facing operational constraints affecting their financial health, the Committee feel that it should not be the ground for levying custom duty on petroleum products for all the refineries so as to increase their refinery gate prices. In regard to need for providing protection to some refineries the Committee desire, as also recommended in the earlier para that an expert group be constituted to go into the constraints faced by these refineries and suitable incentives be provided to these refineries to overcome these constraints. As regards to the taxes imposed by State Governments, the Committee would like the Government to take up the matter with State Governments to rationalize various taxes imposed on these refineries.

The Committee, therefore, while reiterating their earlier recommendation would like the Government to remove custom duty on petroleum products especially for petrol and diesel so as to reduce the refinery gate prices of these products.

E. Revenue from Oil Sector and Differential State Taxes

Recommendation (Sl. No. 6 and 9, Para No. 2.6 and 2.9)

17. The Committee in their recommendation no. 6 noted that contribution to Central Exchequer from petroleum sector has steadily increased from Rs.93513 crore in 2008-09 to Rs.111779 crore in 2009-10 to Rs.136497 in 2010-11 while to State exchequer it has increased from Rs.68285 crore in 2008-09 to Rs.72082 crore in 2009-10 to Rs.88997 in 2010-11. Against the above revenues generated, the pay back by Central Government to OMCs has been inconsistent at Rs.74002 crore in 2008-09 Rs.28792 crore in 2009-10 and Rs.43926 crore in 2010-11 i.e. the payback was of the order of 79%, 26% and 32%. With the rationalization of taxation effective from June 2011 wherein the Government has eliminated 5% custom duty on crude oil and reduced excise duty on diesel from Rs.4.60 per litre to Rs.2 per litre, the revenues of Central Government from oil sector is expected to decline sharply. In this connection the Committee were informed that Central Government has sacrificied Rs.50,000 crore of the total revenue from this sector and the total revenue for 2011-12 is expected to be around Rs.86,000 crore. However, the revenue of State Government which do not share any burden will continue to further rise. The Committee felt that both Centre and State have tendency to bank heavily on this sector to mobilize revenues. However, given the inflationary impact of rise in prices on petroleum products, the Committee were happy at the reduction of taxes and duties by the Central Government as it has positive impact on reducing under-recoveries and help in increasing profitability of oil companies and also bring the prices of petroleum products within a reasonable limit. In the same way the Committee had expected State Government to follow suit and give relief, to common man by bringing down the taxation and forgo some of the revenues.

18. The Committee in their recommendation no. 9 had observed that high State levies are also responsible for high and varied retail selling prices of different petroleum products across the country. The Committee also noted that the Government have requested the State Governments to rationalize their taxes on sensitive petroleum products namely petrol, diesel, PDS kerosene and domestic LPG and also to shift from the ad- valorem tax rates to specific tax component for providing relief to the consumers and as a result, the Government of National Capital Territory of Delhi has reduced the VAT rate on diesel from 20% to 12.5% w.e.f. 20th July 2010. Other States like Bihar, Goa , Tamilnadu and West Bengal have also

reduced Sales Tax on various petroleum products. However, the Committee feel that still there is need to substantially reduce the rates of sales tax on petroleum products and these should be made uniform across the country not only to ensure that consumers get these products at a uniform price but also to contain black marketing in the neighboring areas where different retail pricing of petroleum products exist. The Committee, therefore, recommended that Union Government should seriously pursue the matter with the State authorities at appropriate level and a consensus should be brought to reduce sales tax to a uniform level.

19. In response to the above recommendations, the Ministry of Petroleum & Natural Gas has submitted as below:-

> "All the State Governments have been requested from time to time to reduce the State taxes on sensitive Petroleum products and to give relief to the common man. In response, 17 States /UT have reduced the rate of VAT in the respective States".

20. The Committee in their recommendations had pointed out that the revenue to state Governments has increased from Rs.68285 crore in 2008-09 to Rs.72082 crore in 2009-10 to Rs.88997 crore in 2010-11 and had desired the State Governments to bring down taxation and forgo some of the revenues so as to bring down the prices of petroleum products.

The Committee had also desired that Government should pursue with State Governments to reduce their taxes on petroleum products so as to bring the tax structure in different states to a uniform level.

The Ministry in its reply to the above recommendations has stated that all the State Governments have been requested from time to time to reduce the State taxes on sensitive Petroleum products and to give relief to the common man. In response, 17 States /UT have reduced the rate of VAT in the respective States.

The Committee while appreciating that 17 States/UTs which have reduced the rate of VAT on petroleum products would urge the Ministry that the remaining states should also be persuaded to reduce their taxes with the twin objectives of reducing the prices of petroleum products and to bring parity in the tax structure of different states.

F. Burden Sharing Mechanism and Impact of Under recoveries on financial health of OMCs.

Recommendation (Sl. No. 14, Para No. 2.14)

21. The Committee noted that total burden of under-recovery of OMC's is presently being shared 33% by upstream companies via offering discount in crude oil prices and the remaining burden is apportioned between the Government and the OMCs depending on the feasibility of the Government to allocate funds from budgetary sources and capacity of the OMCs to absorb a part of their under-recoveries. Therefore, the actual burden sharing ratio between the Government and the OMCs varies from year to year on this account. The Committee noted the percentage of under-recoveries born by OMCs was 9% during 2006-07, 21% in 2007-08, Nil in 2008-09, 12% in 2009-10 and 22% in 2010-11. The Committee were constrained to note that not only there is any fixed criteria followed by the Government on the sharing of under –recoveries to the OMCs and the compensation of under-recoveries is also not being received by the companies on time, therefore, their quarterly financial results show very inconsistent results. The Committee had further been informed that the OMCs' mounting under-recoveries have compelled them to borrow heavily, to meet their cash flow requirements and the total borrowings of Rs. 67,332 crore as of March 2008 has ballooned to Rs. 85,933 crore as on 30th June, 2010. The Committee also observed that the combined interest burden of the OMCs during 2009-10 was Rs. 3,441 crore which has also resulted in deteriorating debt equity ratios of OMCs. The Committee, therefore, desired that cash assistance to the OMCs on account of under-recoveries should be transferred at regular intervals on pre- determined basis enabling them to overcome the problems leading to imposition of interest and penalty by tax authorities. The Committee recommended that the Government should evolve a clear and fixed policy to fund under-recovery of OMCs so that estimates of profits of these listed companies where stakes of various investors are also involved, would be properly indicated in the year.

22. The Ministry of Petroleum & Natural Gas has submitted the following reply in this regard:-

> "The amount of under recovery depends on a variety of factors, such as, prices of crude oil and petroleum products in international market, domestic market conditions, etc. So, it is difficult to evolve a fixed policy to compensate the under- recoveries of OMCs. However, every effort is being made to evolve a stable policy to fund under-recoveries of OMCs by the Government to ensure that the cash assistance is received by the OMCs on a regular basis".

23. The Committee had observed that there is no fixed criteria followed by the Government on the sharing of under-recoveries of the OMCs which impact the financial health of the OMCs and had recommended that Government should evolve a clear and fixed policy to fund under-recoveries of OMCs.

The Ministry in its reply have informed that under recoveries depend on variety of factors such as prices of crude oil and petroleum products in international market, domestic market conditions etc and it becomes difficult to formulate a fixed policy to compensate the under-recoveries of OMCs.

The Committee are not convinced of the reply of the Ministry. The Committee would like to be apprised of the precise difficulties being faced by the Ministry in formulating a fixed policy to compensate the under-recoveries of the OMCs on regular periodic intervals.

CHAPTER II

RECOMMENDATIONS/OBSERVATIONS WHICH HAVE BEEN ACCEPTED BY THE GOVERNMENT

Recommendation (Sl. No 1, Para No. 2.1)

The Committee are concerned to note the rising trend of under recoveries of OMCs in the last few years due to high volatility of crude oil price in international market. Since domestic prices of petroleum products are linked with international crude oil prices which is steadily increasing and the Government does not permit passing the impact of full cost of imports on domestic consumers, under recoveries of OMCs have increased from Rs.20,146 crore in 2004-05 to Rs.78190 crore in 2010-11 and is projected to be as high as Rs.1,32,016 crore in 2011-12.

Though the Committee understand that under recoveries do not always signify losses to OMCs, they have put a major dent on the profitability of the companies which in turn have adversely affected their healthy growth and also harmed interests of investors of the company. The rising trend of under recoveries has also posed a major challenge to the Government, who have to on the one hand, see that OMCs work in a competitive atmosphere for healthy growth of this important sector and on the other ensure that common man is not unduly burdened due to inflationary impact of increase in prices of sensitive petroleum products.

The Committee, therefore, desire that Government to tread cautiously in the matter and taking into due consideration of all the stakeholders, devise ways for protecting the interests of the common man.

REPLY OF THE GOVERNMENT

The government is committed to the twin objective of protecting the interest of common man particularly the vulnerable section of the society and also to protect the financial health of the Public sector Oil Marketing Companies (PSU OMCs).

In-spite of the extreme volatility in the prices of crude oil and petroleum products in the international market, in order to protect the consumers from the inflationary impact of high oil prices, the government has fully removed Customs Duty on crude oil and reduced the Customs Duty on Petrol and Diesel from 7.5% to 2.5% and reduced Excise duty on Diesel from Rs. 4.60/ltr. to Rs. 2.00/ltr with effect from 25th June 2011. Further, the Government passed on minimal burden of high prices of crude and petroleum products to the consumers through increase in Retail Selling Price (RSP) of Diesel by Rs. 3/ltr., PDS Kerosene by Rs. 2/ltr. and Domestic LPG by Rs. 50/ Cylinder effective 25th June 2011. Since then there has not been any increase in RSP of these products in the country.

The government is committed to not only protect the interest of common man but also to make available petroleum products of right quality at reasonable prices to the consumers. At the same time, it needs to be appreciated that country's long term energy security depends on the financial health of the OMCs. If their financial health deteriorates on account of the prices under-recoveries, their ability to discharge their assigned task of supplying the entire country with petroleum products would suffer.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part) Dated: 23.03.2012)

Recommendation (Sl. No 5, Para No. 2.5)

The Committee note that expert group constituted under the chairmanship of Dr. Kirit Parikh on current pricing policy of 4 sensitive petroleum products had recommended deregulation of petrol and diesel at both RGP and RSP stage and increase in SKD kerosene and LPG prices.

Further, the Committee have been informed that in consideration of recommendations made by the Export Group, the Government has deregulated the price of petrol and increased the prices of Diesel, Domestic LPG and PDS kerosene with effect from 26th June 2010 which has helped in moderating the under recoveries of OMCs. In this connection the Committee observe from the material furnished by the Ministry that in most of the countries the prices of petroleum products are being regulated to contain the inflationary impact of high oil prices and give relief to their people. The Committee are, therefore, of the view that in our country which still is a growing economy it will not be prudent to deregulate the prices of sensitive petroleum products as it can aggravate inflation and adversely affect the common man. At the same time, the Committee also understand that the under recoveries incurred by the OMCs has detrimental effect on the financial health of these companies and for the robust development of oil sector it is essential for these companies to be able to compete and function in a free and liberalized atmosphere. The Committee, therefore, desire that the Government while refraining from complete deregulation of sensitive petroleum products, should continue with the current policy of compensating OMCs for their under-recovery. The Committee further desire that the Government set up a Study Group to look into the entire gamut of under-recoveries of OMCs and based on which a suitable and clear cut policy should be chalked out so as to timely compensate the OMCs for any losses incurred on this account.

REPLY OF THE GOVERNMENT

With regard to committee's recommendation to set up a study group to look into the issue of under-recoveries, it may be mentioned that the Government had already constituted an Expert Group under the Chairmanship of Dr. Kirit S. Parikh to examine the current pricing policy of the four sensitive petroleum products namely Petrol, Diesel, PDS Kerosene and Domestic LPG and make recommendations for a viable and sustainable pricing policy for these products. The Committee submitted its report on 3rd February 2010.

Based on the recommendations of the committee and decisions taken in the meeting of the Empowered Group on Ministers (EGoM) on 25.06.2010, the Government has already decontrolled the prices of Petrol effective 26th June 2010.

With regard to other sensitive petroleum products, Government is revising the prices periodically to avoid any heavy burden on the consumers and the common man.

The under-recoveries incurred by the Oil Marketing Companies (OMCs) on sale of sensitive petroleum products are being compensated under the 'Burden Sharing Mechanism' approved by the Government. Under the 'Burden Sharing Mechanism', the Central Government is providing cash assistance to the OMCs in addition to the discounts provided by the upstream Oil Companies viz. ONGC, OIL and GAIL. Also, a part of the under-recoveries are being borne by the OMCs themselves. The cash assistance and rate of upstream discounts are being finalized by the Ministry of Finance. The recommendation of the Committee has been noted.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part) Dated: 23.03.2012)

Recommendation (Sl. No 7, Para No. 2.7)

From the material furnished by the Ministry, the Committee note that level of taxation on petroleum products in India vis-à-vis other countries is much lower. In case of petrol it is higher only in respect of countries USA, Canada and Pakistan while in case of diesel, it is the lowest among all countries. In case of PDS kerosene and Domestic LPG, the retail selling price in India is very much lower than all the neighbouring countries. The Committee desire the Government to continue with the existing taxation structure so that the prices of essential items like diesel, LPG, kerosene do not increase to the detriment of the interest of common man.

REPLY OF THE GOVERNMENT

Generally speaking, tax policy of the Government is formulated on a variety of considerations such as need for resources, fiscal condition, ease of administration, demand and supply situation, domestic prices etc. However, Ministry of Finance has noted the suggestion.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part) Dated: 23.03.2012)

Recommendation (Sl. No 10, Para No. 2.10)

The Committee note that high level of taxes on petrol and low taxes on diesel with a subsidy of Rs.10.83 as on 23.12.2011 on sale of each litre of diesel has resulted in big disparity in their retail selling prices. The Committee, however, are of the view that since petrol is consumed mainly by private vehicle users and diesel being used mainly for mass transport system and agriculture etc. there is a merit in keeping the diesel prices at lower level. The Committee note that out of the total consumption of diesel in the country, 15% is used by private car owners, 10% for industrial use and 8% is used in power generation i.e. 33% of diesel is being used by those sections which are taking unfair advantage of low taxation and subsidy on diesel.

The Committee are of the strong view that the Government should take steps to exclude these sectors from the net of beneficiaries of the subsidized diesel. As regards 18% of diesel being used for industrial and power generation, they can be charged unsubsidized prices of diesel.

In regard to use of diesel by private car, the Committee suggest that Government to consider leving a cess on diesel car to be paid at the time of purchase of diesel vehicle and collection of cess should go for compensating the under-recoveries of OMCs.

REPLY OF THE GOVERNMENT

Ministry of Finance had informed that recommendations contained in Para 2.10 of the Committee would be examined as part of proposals for the Budget 2012-13.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part) Dated: 23.03.2012)

Recommendation (Sl. No 12, Para No. 2.12)

The Committee observe that there is a continuous decline in the percentage of household using kerosene but the allocation of kerosene through PDS is intact. Although in States like Andhra Pradesh, Tamilnadu, Maharashtra and Karnataka, there has been considerable increase in LPG enrollment, the Committee do not find any significant decrease in allocation of kerosene through PDS to these States. As the Government intend to enhance LPG coverage in remote and rural part of India with the launch of the Rajiv Gandhi Gramin LPG VitranYojana and Ministry allocate PDS kerosene to different States/UTs on quarterly basis for cooking and illumination only, the Committee recommend that the Union Government should have a stringent monitoring mechanism to control the distribution made to the States and review the allocations periodically so that purpose of helping poor through PDS would be properly served.

REPLY OF THE GOVERNMENT

Kerosene (SKO) is one of the items distributed through Public Distribution System (PDS). Allocation of PDS Kerosene is made by the Government of India to different States/Union Territories (UTs) on a quarterly basis for distribution under PDS for cooking and illumination only. Further, onward distribution within the States/UTs through their PDS network is the responsibility of the concerned States/UTs.

However, in order to rationalize the distribution of PDS Kerosene the quota from 1st quarter of 2010-11 of States/ UTs was restricted on account of increase in Domestic LPG coverage during the first three quarters of 2009-10 (April to December, 2009) and the quantity lapsed on account of non-lifting by States/UTs during the first half of 2009-10. The quota was not reduced in respect of states/UTs having Domestic LPG coverage below the national average namely, Bihar, Chattishgarh, Jharkhand, Madhya Pradesh, Orissa, Puduchery, Rajasthan, Uttar Pradesh and West Bengal.Besides, no reduction was made in respect of J&K, North East States, A&N Islands and UT of Lakshadweep in view of the logistic /special problems being faced by these regions. Quota lapsed during first half of 2009-10 due to non-lifting was reduced in respect of all defaulting states/UTs.

Further, for the year 2011-12, while allocating PDS Kerosene, factors like expansion in domestic LPG penetration (during the period January to December, 2010), lapse of quota allocated during first three quarters of 2010-11 and higher consumption with respect to national average were kept in view. However, the quota was not reduced in respect of states/UTs having Domestic LPG coverage below the national average. Besides, no reduction has been made in respect of J&K, North East States, A&N Islands and UT of Lakshadweep. The quantity lapsed due to non-lifting was reduced in respect of all defaulting states/UTs, wherever applicable.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part)Dated: 23.03.2012)

Recommendation (Sl. No 13, Para No. 2.13)

The Committee are concerned to note that as per study of NCAER, 35% PDS kerosene is diverted for non PDS usage including adulteration, the Committee find that to contain the menace of diversion/black marketing of Superior Kerosene Oil (SKO) distributed under PDS and to ensure that PDS SKO reaches the bonafide beneficiaries, a pilot project on biometric Smart Card based solution for distribution of Domestic LPG and PDS SKO has been launched in the State of Andhra Pradesh in coordination with the Unique Identification Authority of India (UIDAI), the Oil Marketing Companies (OMCs) in the Public Sector and the State Government. In this regard, the Ministry of Petroleum & Natural Gas has signed a Memorandum of Understanding (MOU) with the UIDAI. While appreciating the launching of a Pilot Project for distribution of the Domestic LPG and PDS SKO, the Committee desire that the Pilot Project be completed soon and the Government should create necessary infrastructure to launch similar Projects in all the States and a time bound plan be prepared to implement the same. The Committee would like to be apprised of the action taken and progress made by the Government in this regard.

<u>REPLY OF THE GOVERNMENT</u>

Government has constituted a Task Force in February, 2011 under the Chairmanship of Shri Nandan Nilekani, Chairman, Unique Identification Authority of India (UIDAI) to recommend and implement a solution for direct transfer of subsidies on PDS Kerosene, Domestic LPG and Fertilizer to the intended beneficiaries. As per the terms of reference of the Task Force, the Task Force will study the present mechanism of transfer of subsidies on Kerosene, LPG and Fertilizer, challenges and problems in the governance structures and delivery system. It would examine and suggest an implementable solution for direct transfer of subsidies on Kerosene, LPG and Fertilizers to intended beneficiaries with the use of Aadhaar numbers (Unique Identification numbers), Aadhaar enabled transactions and Aadhaar authentication infrastructure of the UIDAI.

The Chairman, UIDAI has submitted the Interim Report of the Task Force on Direct Transfer of Subsidies on Kerosene, LPG and Fertilizer to Hon'ble Finance Minister on 05th July, 2011. The Interim Report of the Task Force envisages phase-wise implementation for transfer of cash subsidy on Kerosene, LPG and Fertilizer.

The recommendations of the Task Force for direct transfer of cash subsidy on PDS Kerosene and Domestic LPG have been accorded 'in principle' approval by the Empowered Group of Ministers (EGoM) regarding under recovery of the Oil Marketing Companies.

Domestic LPG :

The Government has taken initiatives to launch pilot studies to introduce the changes as proposed in the Interim Report for direct transfer of cash subsidy for domestic LPG, at Hyderabad (Andhra Pradesh) & Mysore (Karnataka). The pilot study has commenced with collecting details of UID number and bank account details of the customers for appending the OMC customer database with Aadhaar and bank details. So far, response from customers has been encouraging in Mysore, whereas it is quite slow in Hyderabad. The system integrator has been appointed who is engaged for designing the network, software and linking of existing transaction software of the oil company with this system. The pilot is executed with active association of UIDAI for requisite technical and specification inputs. The OMC's have reported that from 17.11.2011, trial for delivery of refill after successful authentication of UID details has been started in Mysore, and first such delivery has already taken place.

PDS Kerosene :

The Government has taken initiatives to launch pilot studies to introduce the changes as proposed in the Interim Report for direct transfer of cash subsidy for PDS Kerosene, at Alwar (Rajasthan). Further, this Ministry has invited suggestions from States/UTs Governments for initiating the process for implementing the direct transfer of subsidy in cash for Kerosene. State/UT Governments have been requested to indicate the preparedness of the Public Distribution System (PDS) in the State to undertake this transfer and proposed methodology to be adopted for transferring cash equivalent of subsidy to the bonafide beneficiaries. Further, in order to test the procedure, State/UT Governments have been requested to run a pilot study in two districts/cities/blocks, to be identified by the respective States, before April, 2012, so as to scale it up to the entire State later on.

Ministry of Petroleum & Natural Gas is progressing in line with the recommendations of the Task Force in a phased manner. First Pilot Scheme for direct transfer of cash subsidy on PDS Kerosene has been launched in Kotkasim Tehsil of Alwar District (Rajasthan) w.e.f. 5th December, 2011.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part)Dated: 23.03.2012)

Recommendation (Sl. No 15, Para No. 2.15)

The Committee note that cost of production of crude/barrel by ONGC and OIL is $37.87 and $33.71 per barrel. However, the gross crude oil prices of crude oil has been $89.41 and $86.12/bbl. With discount to OMC of $35.64 and $27.58 per barrel, the net price realised is $53.77 and $58.54 per barrel.The Committee therefore, observe that against the cost of production of ONGC $37.87, the net price realized is $53.77 per barrel i.e. the margin of profit is $15.90 per barrel. Similarly for OIL, against the cost of production of $33.71, the net price realised is $58.54 per barrel i.e. the margin of profit is $24.83 per barrel. The Committee feel that given the high profits being earned by upstream companies, there is a good case of them increasing their contribution in burden sharing of under-recoveries at least to 40% so that will give some respite to OMCs.

REPLY OF THE GOVERNMENT

The amount of under-recovery varies from quarter to quarter as it depends upon a number of variable parameters, such as, price of crude oil and petroleum products in international market, domestic market scenario, etc. Keeping in view all such factors, upstream contribution is being decided by the Government.

The details of sharing of under-recoveries between the Government, Upstream companies and OMCs during last 3 years are given below:

Under-Recovery Sharing

Amount in ` crore

Year	Total U/R	Sharing of Under-Recoveries					
		Government		Upstream Oil companies		OMCs	
		Amount	%	Amount	%	Amount	%
2008-09	103292	71292	69.02%	32000	30.98%	Nil	Nil
2009-10	46051	46051	56.46%	14430	31.33%	5621	12.21%
2010-11	78190	41000	52.44%	30297	38.75%	6893	8.82%
Apr-Dec 2011-12	97,313	45,000	46.24%	36,894	37.91%	15,418	15.84%

As may be seen from the above table, keeping in view the high under-recovery last year, the upstream oil companies' contribution was increased to 38.75% from the normal sharing ratio of around 33%. During the current year i.e. 2011-12, the estimated amount of under-recovery of ` 1,39,659 crore is highest so far, and an appropriate burden sharing mechanism is being worked out. However, for the period between April – December, 2011, upstream Oil Companies have provisionally shared 37.91% of the under recoveries of Public Sector OMCs.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part)Dated: 23.03.2012)

Recommendation (Sl. No 17, Para No. 2.17)

The Committee observe that there is a lot of misgivings among people over the pricing of the petroleum products due to elaborate mechanism and lack of transparency in pricing of these products. The Committee though have been informed that lately the Ministry has started uploading information in the this regard on their website but the Committee feel it is not enough and there is a greater need to make people aware of mechanism of pricing of these products through newspapers and other press media. Also a substantial amount of subsidy is being given on sale of three petroleum products namely diesel, kerosene and LPG for the targeted beneficiaries. The Committee feel that the people in general should also be regularly informed regarding these subsidies and how it is being targeted and utilized. In this way the people would not only be made more aware but also can be vigilant against any misuse of these subsidies by unintended and undeserving beneficiaries

REPLY OF THE GOVERNMENT

The following steps have already been taken to bring transparency in the price mechanism of the sensitive petroleum products:-

1. The buildup of petrol price which has already been decontrolled, is being hosted by OMCs on their website with links to the websites of PPAC and MoP&NG.
2. The International quotes of Crude Price (Indian Basket) and under recovery incurred by OMCs is hosted on the website of PPAC and is updated on daily / fortnightly basis.
3. The Price build-up of Diesel, PDS Kerosene and Domestic LPG at Delhi along with detailed explanation of terms considered in the price build-up is hosted on the website of PPAC and is updated on fortnightly / monthly basis.
4. In addition to the above, the OMCs share all information at the end of each quarter when financial results are announced. Quantum of under-recoveries and subsidy are being communicated to the general public by OMCs through Press Conferences. Further, on several occasions, the subject of under-recovery, subsidy and pricing philosophy is discussed in detail in different forums, including media interactions, so that the public at large is aware of the issues impacting pricing of petroleum products and Government subsidies.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part)Dated: 23.03.2012)

CHAPTER III

RECOMMENDATIONS/OBSERVATIONS WHICH THE COMMITTEE DO NOT DESIRE TO PURSUE IN VIEW OF THE GOVERNMENT'S REPLIES

Recommendation (Sl. No 16, Para No. 2.16)

The Committee note with concern that special oil bonds issued in part compensation of under-recoveries of the public sector Oil Marketing Companies (OMCs) has to be generally sold at a discount and can only be used for capital expansion plans provided there is adequate internal resources available for financial working capital during the intervening period. The Committee are further surprised to know that although the bonds issued by the Government to OMCs are considered as an eligible security or investment by Provident Fund(PFs) and Insurance companies, they do not have Statutory Liquidity Ratio (SLR) status and as a result banks are unwilling to buy such bonds from OMCs. Thus, the market and appetite for oil bonds is limited. In view of the forgoing, the Committee find that the special oil bonds issued by the Government are unable to solve cash liquidity problems which force the companies to borrow from market at high rate of interest to meet their regular cash requirements. Therefore, the Committee strongly recommend that oil bonds being issued by the Government should be given SLR status so that OMCs should not have to wait for suitable opportunity for disposal of bonds in the market and can sell these bonds to the banks. The Committee also recommend that as the insurance sector is a good source of revenue generation for the Government, insurance companies may be requested to invest their surplus funds in oil bonds issued by the Government to fund under-recovery.

REPLY OF THE GOVERNMENT

Since the Oil Bonds issued by Government to OMC's do not have SLR status, the practice of issuance of Oil Bonds under 'Burden Sharing Mechanism' has been stopped and since 2009-10 only cash assistance is being provided to OMCs towards compensation of under-recoveries.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part)Dated: 23.03.2012)

CHAPTER IV
RECOMMENDATIONS/OBSERVATIONS IN RESPECT OF WHICH REPLIES OF THE GOVERNMENT HAVE NOT BEEN ACCEPTED BY THE COMMITTEE

Recommendation (Sl. No 2, Para No. 2.2)

The Committee note that during 1976-2002, pricing of sensitive petroleum products was based on Administrative Pricing Mechanism (APM). Under APM, cost of Crude oil processed by Refineries was fixed taking into account the delivered cost of crude oil and the normative refining cost. Further, besides normative marketing and distribution costs, Oil Marketing Companies (OMCs) were also allowed 12% post-tax returns. The Committee have been informed that the APM was reported to be increasingly unsuitable for the long term growth and efficiency of oil industry due to lack of adequate financial resource generation and incentives for investment in technological upgradations or cost minimization and for achieving consumer friendly and competitive vibrant petroleum sector. As such APM was fully dismantled with effect from 1st April 2002 and since then refinery gate prices of four sensitive petroleum products viz. petrol, diesel, LPG and kerosene are being governed by IPP/TPP which includes beside FOB price of petroleum products in the Arab Gulf, other components namely ocean freight, custom duty, insurance charges etc. in case of IPP and advance licensing benefits in case of EPP.

While going into merits of cost plus mechanism and TPP/IPP mechanism, the Committee were informed that actual cost of refinery/production of individual product was not identifiable separately due to operational procedures and TPP/IPP mechanism based on widely traded and international market price reflect the competitive conditions and help refineries to optimize turnover and over and above cost. The Committee while accepting the contentions of the Ministry for going in TPP/IPP mechanism are, however, of the view that when the refinery gate prices has been aligned to international market prices there is no justification of including other costs in TPP/IPP on the reasons that these costs have been incurred by refineries while importing crude oil.

Moreover the value of these components is less than 2% of the finished product cost and the refineries will not be much affected on exclusion of these components from the refinery gate prices.

The Committee, therefore, strongly recommend that the components other than FOB price of petroleum products at Arab Gulf should not be included in the refinery gate price which will bring down the cost of petroleum products and consequently reduce the under recoveries of OMCs.

REPLY OF THE GOVERNMENT

As per the current pricing mechanism, the Refinery Gate Price (RGP) of Petrol and Diesel is determined based on Trade Parity Price (as per the recommendations of Rangarajan Committee Report) whereas the RGP of PDS

Kerosene and Domestic LPG is determined based on Import Parity Price. Based on the RGP effective 16th January 2012 for Petrol and Diesel and 1st January 2012 for PDS Kerosene and Domestic LPG, the impact of elements of customs duty, ocean freight, insurance charges, ocean loss, LC Charges and port dues etc. included in RGPs at Mumbai is given below:

	Petrol	Diesel	PDS Kerosene	Domestic LPG
Elements included in RGP	1,097	1,219	222	306
RGP	39,710	44,633	40,641	43,819
%	2.76%	2.73%	0.55%	0.70%

(Rs. / KL)

As may be seen from the above table, with the gradual reduction in the customs duty on crude and POL products, the current impact of elements (other than FOB) in the RGP is only around 0.5% to 2.8%. This ensures that refineries recover their cost of imports of raw material and also various other levies i.e. octroi, entry tax etc. on the refineries.

Hence RGP based on FOB would not cover the cost of refining crude oil particularly by the existing older refineries of PSU OMCs and would not be adequate to meet their CAPEX requirements towards capacity addition, quality up-gradation, etc.
In view of the above, it is not advisable to fix the RGP of petroleum products at FOB price.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part)Dated: 23.03.2012)

Comments of the Committee

(Please see Para 7 of the Chapter-I)

Recommendation (Sl. No 3, Para No. 2.3)

The Committee note that the petroleum products prices in the international market do not always move in tandem with the crude oil prices but depend on the demand and supply constraints, seasonal fluctuations etc. The Committee have also been informed that out of 9 to 10 products that are produced from crude oil, three products are priced above crude oil prices and rest are traded below the crude prices. Moreover, there is around 10% fuel loss in processing of crude oil which increases the cost price of the finished products.

On consideration of the material submitted and deposition by representatives, the Committee are convinced that in current international marketing scenario where there are narrow margins, the Indian refineries have to be very efficient in order to compete and be viable and profitable. The Committee, however, find that the public sector refineries are mostly of small capacity and suffer from inherent disadvantages like locational

disadvantages, old technologies which has adversely affected the GRM of the refineries.

The Committee were further informed that BPCL, Mumbai are paying 3% octroi to BMC for bringing crude oil to refinery. So far Rs.1140 crore are being paid annually on this account which has denied the profitability of the company.

The Committee recommend that expert group be constituted to evaluate the performance of each refinery taking into account various constraints faced by them and take effective steps to make them more efficient, viable and profitable.

REPLY OF THE GOVERNMENT

The Recommendation of the Committee has been noted for necessary action.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part) Dated: 23.03.2012)

Comments of the Committee
(Please see Para 10 of the Chapter-I)

Recommendation (Sl. No 8, Para No. 2.8)

The custom duty levied on the petroleum products which was 7.5% and subsequently revised to 2.5% in June, 2011 does not actually add to the revenues of the Government as product imports are almost nil owing to surplus refining capacity in the Country. Instead, the Committee understand that it goes in to the calculation of fixing the import parity prices of these products at international level which in turn increases consumer price. The Committee, therefore, recommend that the custom duties on petroleum products especially that on petrol and diesel be brought down to Nil from the present level of 2.5% to make it at par with the custom duty on crude oil which at present is Nil leaving no room for calculation of Refinery Gate price which is the average of 80% of Import Parity Price (IPP) and 20% of Export Parity Price (EPP). The Committee would also like to be apprised in cost reduction of petroleum products at refinery level after recent decision of the Government to remove the entire custom duty on crude oil and how this would help in bringing down the refinery gate price.

REPLY OF THE GOVERNMENT

The effective rate of protection on Petrol and Diesel has come down from 10% in 2002 to 2.5% currently. In fact, the Customs Duty on other major petroleum products namely PDS Kerosene, Domestic LPG and ATF is NIL.

Thus, the remaining small effective rate of protection available is essential to provide some level of protection to refineries most of which are in operation for a long period.

The refineries also incur irrecoverable taxes imposed by various State Governments which are offset by the effective rate of protection to ensure viability in refinery operations.

As regards the impact of recent reduction in Customs Duty on crude oil and petroleum products in June 2011 on Refinery gate price of the Petroleum products, the reduction in Refinery Gate Price is Rs.1.75 per litre on Petrol and Rs.1.87 per litre on Diesel at Mumbai.

Further, reduction in Customs Duty on crude oil and petroleum products in June 2011 has adversely affected the profitability of four North East refineries. This is due to the fact that the North East refineries do not process imported crude oil. Therefore, crude procurement cost for the North East refineries does not reduce corresponding to reduction in Customs Duty on crude oil.On the other hand, reduction in Customs Duty on products has brought down the Refinery Gate Prices leading to lesser sales realization. Hence any further reduction in Customs Duty on petroleum products, especially petrol and diesel would further worsen the deteriorating financial situation of the North East refineries that had arisen after duty restructuring in June, 2011.

It is also added that a 2.5% differential between basic Customs Duty on crude oil and petroleum products, is based on the recommendation of the Rangarajan Committee on pricing and Taxation of Petroleum, to provide a viable margin to domestic refineries.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part) Dated: 23.03.2012)

Comments of the Committee
(Please see Para 16 of the Chapter-I)

Recommendation (Sl. No 14, Para No. 2.14)

The Committee note that total burden of under-recovery of OMC's is presently being shared 33% by upstream companies via offering discount in crude oil prices and the remaining burden is apportioned between the Government and the OMCs depending on the feasibility of the Government to allocate funds from budgetary sources and capacity of the OMCs to absorb a part of their under-recoveries. Therefore, the actual burden sharing ratio between the Government and the OMCs varies from year to year on this account.The Committee note the percentage of under-recoveries born by OMCs was 9% during 2006-07, 21% in 2007-08, Nil in 2008-09, 12% in 2009-10 and 22% in 2010-11. The Committee are constrained to note that not only there is any fixed criteria followed by the Government on

the sharing of under –recoveries to the OMCs and the compensation of under-recoveries is also not being received by the companies on time, therefore, their quarterly financial results show very inconsistent results. The Committee have further been informed that the OMCs' mounting under-recoveries have compelled them to borrow heavily, to meet their cash flow requirements and the total borrowings of Rs. 67,332 crore as of March 2008 has ballooned to Rs. 85,933 crore as on 30th June, 2010.

The Committee also observed that the combined interest burden of the OMCs during 2009-10 was Rs. 3,441 crore which has also resulted in deteriorating debt equity ratios of OMCs. The Committee, therefore, desire that cash assistance to the OMCs on account of under-recoveries should be transferred at regular intervals on pre- determined basis enabling them to overcome the problems leading to imposition of interest and penalty by tax authorities. The Committee recommended that the Government should evolve a clear and fixed policy to fund under-recovery of OMCs so that estimates of profits of these listed companies where stakes of various investors are also involved, would be properly indicated in the year.

REPLY OF THE GOVERNMENT

The amount of under recovery depends on a variety of factors, such as, prices of crude oil and petroleum products in international market, domestic market conditions, etc. So, it is difficult to evolve a fixed policy to compensate the under- recoveries of OMCs. However, every effort is being made to evolve a stable policy to fund under-recoveries of OMCs by the Government to ensure that the cash assistance is received by the OMCs on a regular basis.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part) Dated: 23.03.2012)

Comments of the Committee
(Please see Para 23 of the Chapter-I)

CHAPTER V

RECOMMENDATIONS/OBSERVATIONS IN RESPECT OF WHICH FINALREPLIES OF THE GOVERNMENT ARE STILL AWAITED

Recommendation (Sl. No 4, Para No. 2.4)

The Committee noted with concern that although shipping strategy of oil companies has always been to maximize transportation of imported crude oil in Very Large Crude Carriers(VLCC) there are infrastructure constraints like draft restrictions and port jetty limitations at Mumbai port which do not allow VLCCs to berth in Mumbai. Hence, refineries in Mumbai are constrained to import crude oil through smaller size of vessels. The Committee have also been informed that at Visakhapatnam, the Single Point Mooring (SPM) system, which is going to start soon will enable receipt of crude oil through VLCC's. Considering the facts that Very Large Crude Carriers (VLCC), a widely used crude oil carrier that can carry about 270 TMT of crude oil and will be more economical in regard to volume of transporting imported crude, the Committee feel that infrastructure constraints like draft restrictions and port jetty limitations at Mumbai Port should have been addressed on urgent basis. The Committee, urge the Ministry to take up the matter with the appropriate authorities to ensure that the required infrastructure to handle VLCC be built at all the ports off-loading crude oil at the earliest.

REPLY OF THE GOVERNMENT

Upgrading infrastructure facilities for imports is a continuous process and is being pursued keenly by all stakeholders.Presently,following actions have been taken/ are being taken in this regard:

(i) Single Point Mooring (SPM) facility at Visakhapatnam Refinery of HPCL has been commissioned in February, 2011.
(ii) SPM facility off Mangalore Coast and other auxiliary facilities including Buoy, Sub-sea pipeline, Booster pumping station and pipelines to refinery from the Strategic Storage facility is under construction at Mangalore and from booster pumping station to MRPL Coastal terminal, the mechanical completion shall be achieved by the end of 2012.
(iii) Integrated Offshore Crude handling facilities project at Paradeep shall be completed by the end of 2012, ahead to completion of Paradeep Refinery.

(iv) Crude Oil import infrastructure at West Coast by IOCL is under review.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part) Dated: 23.03.2012)

Comments of the Committee

(Please see Para 13 of the Chapter-I)

Recommendation (Sl. No 6, Para No. 2.6)

The Committee note that contribution to Central Exchequer from petroleum sector has steadily increased from Rs.93513 crore in 2008-09 to Rs.111779 crore in 2009-10 to Rs.136497 in 2010-11 while to State exchequer it has increased from Rs.68285 crore in 2008-09 to Rs.72082 crore in 2009-10 to Rs.88997 in 2010-11. Against the above revenues generated, the pay back by Central Government to OMCs has been inconsistent at Rs.74002 crore in 2008-09 Rs.28792 crore in 2009-10 and Rs.43926 crore in 2010-11 i.e. the payback was of the order of 79%, 26% and 32%. With the rationalization of taxation effective from June 2011 wherein the Government has eliminated 5% custom duty on crude oil and reduced excise duty on diesel from Rs.4.60 per litre to Rs.2 per litre, the revenues of Central Government from oil sector is expected to decline sharply. In this connection the Committee were informed that Central Government has sacrificied Rs.50,000 crore of the total revenue from this sector and the total revenue for 2011-12 is expected to be around Rs.86,000 crore. However, the revenue of State Government which do not share any burden will continue to further rise.

The Committee feel that both Centre and State have tendency to bank heavily on this sector to mobilize revenues. However, given the inflationary impact of rise in prices on petroleum products, the Committee are happy at the reduction of taxes and duties by the Central Government as it has positive impact on reducing under- recoveries and help in increasing profitability of oil companies and also bring the prices of petroleum products within a reasonable limit.In the same way the Committee would expect State Government to follow suit and give relief, to common man by bringing down the taxation and forgo some of the revenues.

REPLY OF THE GOVERNMENT

All the State Governments have been requested from time to time to reduce the State taxes on sensitive Petroleum products and to give relief to the common man. In response, 17 States/UT have reduced the rate of VAT in the respective States.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part) Dated: 23.03.2012)

Comments of the Committee
(Please see Para 20 of the Chapter-I)

Recommendation (Sl. No 9, Para No. 2.9)

The Committee observe that high State levies are also responsible for high and varied retail selling prices of different petroleum products across the country. The Committee also note that the Government have requestedthe State Governments to rationalize their taxes on sensitive petroleum products namely petrol, diesel, PDS kerosene and domestic LPG and also to shift from the ad- valorem tax rates to specific tax component for providing relief to the consumers and as a result, the Government of National Capital Territory of Delhi has reduced the VAT rate on diesel from 20% to 12.5% w.e.f. 20th July 2010. Other States like Bihar, Goa, Tamilnadu and West Bengal have also reduced Sales Tax on various petroleum products. However, the Committee feel that still there is need to substantially reduce the rates of sales tax on petroleum products and these should be made uniform across the country not only to ensure that consumers get these products at a uniform price but also to contain black marketing in the neighbouring areas where different retail pricing of petroleum products exist. The Committee, therefore, recommend that Union Government should seriously pursue the matter with the State authorities at appropriate level and a consensus should be brought to reduce sales tax to a uniform level.

REPLY OF THE GOVERNMENT

All the State Governments have been requested from time to time to reduce the State taxes on sensitive Petroleum products and to give relief to the common man. In response, 17 States/UT have reduced the rate of VAT in the respective States.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part) Dated: 23.03.2012)

Comments of the Committee
(Please see Para 20 of the Chapter-I)

Recommendation (Sl. No 11, Para No. 2.11)

The Committee have been informed that in addition to the Government subsidy on domestic LPG and PDS Kerosene, the Government upstream oil companies and OMCs are also shouldering a part of the subsidy by not passing the full impact of increase in the price of petroleum products to the domestic consumers. In view of the huge burden of subsidy, all Central duties on PDS SKO and domestic LPG were abolished since 1.3.2005. The under recoveries on PDS SKO and domestic LPG for the year 2010-11 is Rs.19,485 crore and Rs.21,772 crore respectively which is more than 50% of total under recoveries. The Committee in their 8th report on Demands for Grants (2011-12) of the

Ministry of Petroleum and Natural Gas have already recommended that to offset the huge losses made on account of subsidized domestic LPG cylinders, the Government may consider to do away with providing subsidized LPG to rich and affluent people having an income of more than Rs.6 lakh per annum including those holding constitutional posts, public representatives like MPs, MLAs/MLCs. The Committee reiterate its earlier recommendation to address huge under recovery made on account of domestic LPG and PDS kerosene.The Committee would like to know the action taken by Government in this regard.

REPLY OF THE GOVERNMENT

Capping of Subsidy on Domestic LPG is subject to policy approval by the Government. The Government is yet to take a decision in the matter.

With respect to Kerosene, during 2011-12, PDS Kerosene quota for the States/UTs was rationalized on account of (i) increase in Domestic LPG coverage (during January to December, 2010) in respect of all the States/UTs excluding North East States, island territories, J&K and States having coverage of Domestic LPG below national average; (ii) PDS Kerosene quota lapsed (during first three quarters of 2010-11) on account of non-upliftmentby States/UTs; (iii) adjustments in the quota keeping in view higher per capita allocation of PDS kerosene to certain States/UTs during the previous year. Accordingly, the allocation of PDS Kerosene was rationalized, and the overall allocation for 2011-12 was reduced by 7.9% in comparison to the allocation of 2010-11.

(M/o Petroleum & Natural Gas O.M. No.P-20012/11/09-PP (Vol.I) (Part) Dated: 23.03.2012)

New Delhi;
August, 2012
Bhadrapada,1934 (Saka)

ARUNA KUMAR VUNDAVALLI,
Chairman,
Standing Committee on
Petroleum & Natural Gas.

Annexure-I

MINUTES
STANDING COMMITTEE ON PETROLEUM & NATURAL GAS
(2011-12)
FOURTEENTH SITTING
(27.08.2012)

The Committee sat on Monday the 27th August, 2012 from 1500 hrs. to 1700 hrs. in Committee Room 'D', Parliament House Annexe, New Delhi.

PRESENT

Shri Aruna Kumar Vundavalli - Chairman

MEMBERS

Lok Sabha

2 Shri Sanjay Singh Chauhan
3 Smt. Santosh Chowdhary
4 Shri Kalikesh N. Singh Deo
5 Shri Mukeshkumar Bheravdanji Gadhvi
6 Dr. Thokchom Meinya
7 Shri Mahabal Mishra
8 Shri Kabindra Purkayastha
9 Shri M.B. Rajesh
10 Shri C.L. Ruala
11 Shri Dhananjay Singh
12 Shri Uday Pratap Singh
13 Shri Sudarshan Bhagat

Rajya Sabha

14 Smt. Gundu Sudharani
15 Dr. Prabha Thakur
16 Shri Pankaj Bora
17 Shri Tapan Kumar Sen
18 Shri Shankarbhai N. Vegad
19 Shri Mansukh L. Mandaviya

Secretariat

1. Shri A.K.Singh - Joint Secretary
2. Smt. Anita Jain - Director
3. Shri H. Ram Prakash - Deputy Secretary

2. At the outset, Hon'ble Chairman welcomed the representatives of the Ministry of Petroleum and Natural Gas and other organizations to the sitting of the Committee.

3. **** **** **** **** **** **** **** **** **** **** ****

4. The Committee then considered and adopted the draft Action Taken Report on the subject 'Challenges of Under-recoveries of Petroleum Products' without any modification. The Committee also authorized the Chairman to present the Report to both Houses of Parliament.

5. A verbatim record of the proceedings of the sitting has been kept.

The Committee then adjourned.

---

*Matter not related to the subjec

Annexure II

(Vide Para 4 of the Introduction)

ANALYSIS OF THE ACTION TAKEN BY THE GOVERNMENT ON THE RECOMMENDATIONS CONTAINED IN THE NINTH REPORT (FIFTEENTH LOK SABHA) OF THE STANDING COMMITTEE ON PETROLEUM AND NATURAL GAS (2011-12) ON 'CHALLENGES OF UNDER-RECOVERIES OF PETROLEUM PRODUCTS'.

I	Total No. of Recommendations	17
II	Recommendations/Observations which have been accepted by the Government (Vide Recommendations at Sl. Nos. 1, 5, 7, 10, 12, 13 ,15 and 17.)	8
	Percentage to Total	47%
III	Recommendations/Observations which the Committee do not desire to pursue in view of Government's Reply (Vide Recommendations at Sl. No. 16)	1
	Percentage of Total	6%
IV	Recommendations/Observations in respect of which replies of the Government have not been accepted by the Committee (Vide Recommendations at Sl. Nos. 2, 3, 8 and 14.)	4
	Percentage of Total	23.5%
V	Recommendations/Observations in respect of which final replies of the Government are still awaited (Vide Recommendations at Sl. Nos. 4 ,6, 9 and 11)	4
	Percentage of Total	23.5%