NINTH REPORT

STANDING COMMITTEE ON PETROLEUM & CHEMICALS (1994-95)

(TENTH LOK SABHA)

PRICING OF PETROLEUM PRODUCTS

(MINISTRY OF PETROLEUM & NATURAL GAS)

Presented to Lok Sabha on 19 DEC 1994
Laid in Rajya Sabha on 19 DEC 1994

LOK SABHA SECRETARIAT
NEW DELHI
November, 1994/Kartika, 1916 (Saka)

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CORRIGENDA TO NINTH REPORT OF STANDING COMMITTEE ON PETROLEUM & CHEMICALS ON 'PRICING OF PETROLEUM PRODUCTS'.

Page	Para	Line	
Contents page	-	3	After "Composition of the Committee..(iii Insert "Introduction ....(v"
2	4(d)	5	For "in essential use" Read "inessential use"
7	19	1-2	For " as a matter that of principle" Read "that as a matter of principle"
30	6	3	For "royalty 20% " Read "royalty @ 20% "
31	8	16	For "completion on-going" Read "completion of on-going"
32	10	15	For "we" Read "to"

CONTENTS

PAGE

COMPOSITION OF THE COMMITTEE .... (iii)

PART I

BACKGROUND ANALYSIS

I. HISTORICAL DEVELOPMENTS 1

II. PRICING OF CRUDE OIL 3

(a) Pricing of Indigenous Crude 3

(b) Cess 5

(c) Cost of Imported Crude 8

(d) Royalty 8

III. REFINING COST 9

IV. EFFICIENCY OF PIPELINES NETWORK 16

V. MARKETING AND PRICING MECHANISM 20

VI. PARALLEL MARKETING 26

PART II

RECOMMENDATIONS/CONCLUSIONS OF THE COMMITTEE 28

COMPOSITION OF THE STANDING COMMITTEE ON PETROLEUM AND CHEMICALS (1994-95)

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---

*Ceased to be Member of the Committee consequent upon retirement from Rajya Sabha *w.e.f.* 1st July, 1994. Renominated to the Committee *w.e.f.* 12th July, 1994.

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***Expired on 21st September, 1994.
$Nominated to the Committee *w.e.f.* 8th April, 1994.
$$Nominated to the Committee *w.e.f.* 11th April, 1994.

INTRODUCTION

I, the Chairman of Standing Committee on Petroleum & Chemicals (1994-95) having been authorised to submit the Report on their behalf, present this Ninth Report on the Ministry of Petroleum and Natural Gas relating to "Pricing of Petroleum Products".

2. The Committee took evidence of the representatives of Ministry of Petroleum and Natural Gas at their sittings held on 29th June and 15th July, 1994.

3. The Committee considered and adopted the Report at their sitting held on 18th October, 1994.

4. The Committee wish to express their thanks to the officers of the Ministry of Petroleum and Natural Gas for placing their considered views before the Committee on the subject.

NEW DELHI:
November 7, 1994
Kartika 16, 1916, (Saka)

SRIBALLAV PANIGRAHI
Chairman,
Standing Committee on
Petroleum & Chemicals.

PART I

BACKGROUND ANALYSIS

I. Historical Developments

The first attempt to regulate the oil prices was based on Valued Stock Account (VSA) procedure agreed to between the Government of India and Burmah Shell in 1950. Subsequently, following the examination of the price structure of the petroleum products by the Chief Cost Accounts Officer, Government of India, a new *ad-hoc* arrangement was entered into from Ist April, 1959. The first systematic attempt to regulate the prices of petroleum products was based on the recommendations of the Damle Committee, 1961. This Committee was the precursor of several other Committees set up by the Government from time to time to regulate oil prices.

2. The Damle Committee, 1961 and the Talukdar working Group, 1965 recommended fixing of the prices of petroleum products on import parity basis as the bulk of the crude oil and major petroleum products were being imported into the country from West Asia. The Shantilal Shah Committee, 1969, however, did not favour import parity as a concept, as indigenous crude oil production and refined capacity had become a considerable factor by that time. However, import parity had to continue because of the commitments made to the foreign oil companies in the "refinery agreements" under which they had set up the refineries in India. The Shantilal Shah Committee also fixed the norms for marketing margins and profits in respect of each product.

3. The Oil Prices Committee (OPC) 1976 recommended discontinuance of the import parity principle and recommended that the pricing of major petroleum products at the refinery point be based on domestic cost, i.e. retention concept, by taking the delivered cost of crude oil, the cost of refining of crude oil and reasonable return on the capital employed. They also recommended the retention concept for the marketing activities. The retention concept was implemented for determining the ex-refinery prices from 14th July, 1975 when the Government accepted the Interim Report of the OPC. This principle was extended to the marketing activity from 16th December, 1977 when Governnet implemented the final recommendations of the OPC 1976.

4. The existing system of pricing of petroleum products is based on Oil Prices Committee (OPC) (1976) as amended by the Oil Cost Review

Committee (1984). The salient features of the existing system of pricing of petroleum products are as under:—

(a) The pricing of petroleum products for the refining and marketing units is based on the retention concept whereunder oil refineries, oil marketing companies and the pipelines are compensated operating costs and return @ 12% post tax net worth.

(b) The ex-storage ceiling selling prices are uniform at all the refineries.

(c) For consumers, the selling price of a product is arrived at by adding the applicable freight from the oil refinery to the Depot and from Depot to the Retail Outlets or direct consumers. Dealers commission wherever applicable is also added.

(d) The prices of certain petroleum products like Kerosene, LPG (domestic) and feed stocks for fertiliser units are subsidised for socio-economic reasons. Similarly, fuels like Petrol, ATF, LPG for industrial use are priced above the cost of production to discourage their in essential use.

(e) The prices of petroleum products are reviewed and revised from time to time to see that pool accounts are balanced.

5. Another Oil Prices Review Committee (OPRC) was constituted by the Ministry of Petroleum and Natural Gas, Govt. of India in September, 1989 to examine the indigenous crude oil prices, prices of petroleum products and allied matters relating to crude oil movement, measurement, quality etc. after taking into account all the relevant factors including the resources requirement of crude oil producers, reasonable returns to oil companies. The Committee submitted its Report in June, 1991. During the course of examination the Committee enquired whether the Ministry had taken any decision on the recommendations of the 1991 Report. The Petroleum Secretary stated:

> "We took a view in this regard. This was nacessary in connection with some of the indications we had to give to the A.D.B. Hence, at that point of time, we took a view that we will not process this report further. We decided to take separate decisions regarding reasonable compensation to oil companies etc. We said we will depend on the 1984 report where there is a formula for production cost etc."

He added:—

> "The situation is totally different now. After this Committee was appointed, a number of products were going out of administered price system. More and more refinery investments are being made. When we locate a refinery or a bottling plant, a total logistical study is made to optmise the use and to find out which is best location etc. Today, under free licencing system, a private investor can set up a refinery wherever he feels. This will disturb totally the optimised logistics of our system. If you go and try to compensate oil companies on a system which will not have any resemblance to ground reality, it will lead to problems. We said let us pursue

> whatever action is required based on 1984 report which has given a formula to update cost every three years."

6. When asked further as to whether the implementation of OPRC Report, 1991 could help in bringing down the prices of petroleum products, the witness stated:—

> "There was no point in jacking up the prices. We thought that whatever cost is legitimate — cost escalations were there — that should be given under the 1984 report. We are able to take care of some of the basic issues like crude oil price."

II. Pricing of Crude Oil

(a) Pricing of Indigenous Crude

7. Prior to 1981, crude oil prices were fixed on various considerations like import parity, long run social marginal cost etc. In 1981, Government revised system of the crude oil pricing departing from the OPC concepts. Thereafter the prices of indigenous crude oil were unchanged till 1992 when the Cabinet Committee on Infrastructure reviewed the crude pricing and observed that due to urremunerative price of indigenous crude oil, ONGC and OIL were unable to generate resources for developing more oil fields and exploration in new areas. The Cabinet Committee recommended that domestic well head price of crude oil should be so determined as to compensate ONGC and OIL for the cost of production and reasonable return on investment, i.e. the well head price of the crude oil is weighted average of cost of production of ONGC and OIL plus 15% return net of tax on capital employed. In addition to the price paid to the ONGC/OIL a cess at the rate of Rs. 900/- MT. royalty at the rate of Rs. 528/- MT (i.e. 20% on well head price plus cess) and sales tax at the rate of 4% is borne by the refineries. The final price payable by refineries w.e.f. 1.4.93 is as under:—

	Price payable (provisional)	(Rs./MT)
(a)	Average cost of production payable to ONGC/OIL including return	1741
(b)	Cess	900
(c)	Royalty @20% (a+b)	528
(d)	Sales tax @ 4%	127

8. Oil & Natural Gas Corporation Ltd. (ONGC) and Oil India Ltd. (OIL) are two public sector undertakings under the administrative control

of the Ministry of Petroleum & Natural Gas which are engaged in exploration and production of oil and gas. The cost of crude oil production of ONGC and OIL during last three years was as under:—

(Cost: Rs./Tonne)

Year	ONGC	OIL
1991-92	917	571.51
1992-93	1116	717.12
1993-94 (Provisional)	1124	781.11

9. During the course of evidence the Committee enquired about the reasons for difference in cost of production of ONGC and OIL. The Petroleum Secretary stated:

> "Generally on-shore costs are low and off-shore costs are high. In ONGC, two-thirds of oil is coming from off-shore projects. ONGC's costs are more. Oil India Limited has all the projects on-shore only."

10. Asked about the steps taken by these two oil producing companies to reduce their cost of production, the Ministry of Petroleum & Natural Gas replied in a note that the steps taken to reduce the cost of crude oil production by ONGC and OIL include application of value engineering techniques, controlling over-head and semi-variable expenditure, use of latest technology and introduction of improved managerial techniques etc. Besides, other steps *inter-alia* include:—

(i) Improvement of productivity, thereby, reduction in unit costs of production.

(ii) Improvment in time taken for completion of various jobs by progressive monitoring and reporting.

(iii) Effective training to ensure efficiency at all levels leading to higher productivity.

(iv) Successful implementation of effective preventive maintenance schemes.

(v) Optimum utilization of equipments.

(vi) Constant look out for alternative methods for performing a job better in order to improve productivity.

(vii) Standardization of the specifications of materials and stores consumables without jeopardising job requirements and effects to optimise consumption of stores through R&D.

(viii) Curtailment of essential and non-essential expenditure so however, that only production oriented expenditure are accorded priority.

(ix) Control over overhead costs by effecting reduction in travelling, entertainment, non-essentials expenditure, training, books and periodicals, services etc.

(x) Effecting capital rationing by techno-economic feasibility analyses of all expenditure in schemes costing Rs. 50 lakhs and above and repriotisation of expenditure in value adding schemes.

(xi) Effective control and monitoring of safety environmental and pollution aspects to obviate untowardly outgoes on account of any mishaps.

(xii) Upgradation of technology to reduce operating costs.

(b) Cess

11. Apart from cost of production of crude oil, the second largest component is cess. The Committee wanted to know the basis for imposing such high cess on crude oil which ultimately lead to steep price escalation in petroleum products. The Petroleum Secretary informed that the cess was being collected under the provisions of Oil Industry (Development) Act, 1974. Explaining the objectives for cess collection, the witness stated:—

> "The whole purpose of introducing this cess was that at that time, we were an oil deficient country. The intention was that the country should become self-sufficient in oil production but, in general, oil development. So, the Parliament enacted a law called the Oil Industry Development Cess Act under which a cess is collected on every tonne of oil that is produced."

12. Section 15 of Oil Industry (Development) Act, 1974 provides for collection of cess on production of crude oil and natural gas at a rate fixed by the Govt. from time to time. The present rate is Rs. 900/- per tonne on crude oil and Rs. 300 per thousand cubic metres for natural gas. Section 16 of the Act provides that "the proceeds of the duties of excise levied under section 15 shall first be credited to the Consolidated Fund of India and the Central Government may, if Parliament by appropriation made by law in this behalf so provides, pay to the Board from time to time, from out of such proceeds, after deducting the expenses of collection, such sums of money as it may think fit for being utilised exclusively for the purposes of this Act."

13. The Committee enquired about the quantum of cess collection under the provisions of Oil Industry (Development) Act, 1974 and the amount given to Oil Industry Development Board (OIDB) for giving loans/grants to Oil Companies for promoting the oil industry. The Petroleum Secretary apprised the Committee that out of about Rs. 20,000 crores collected under the provisions of the Act since its enactment, and amount of Rs. 902 crores has only been released to OIDB so far.

14. The Oil Industry Development Board (OIDB) set up under the provisions of the Oil Industry (Development) Act, 1974 provides financial assistance for the development of oil industry. The financial assistance is extended by way of loans and grants for projects, R&D etc. necessary for the development of oil industry. The OIDB also extends term loans for meeting the capital expenditure on approved projects for the development of oil industry. Assistance is granted for acquisition of fixed assets, setting up of new units as well as for the expansion, modernisation, renovation schemes of the existing units and programmes connected with the exploration, production, refining and storage of crude oil. Further, loans on soft terms and grants-in-aid are given for scientific, technological and economic research activities for the development of the oil industry. The OIDB has disbursed loans and grants to the extent of Rs. 5175 crores and Rs. 93 crores respectively, on a cumulative basis upto 31st March, 1994 to various organisations engaged in the oil industry.

15. The following table shows the trend of cess collection made by the Central Government and allocation made to OIDB during the last three years:—

Year	Collection of cess on crude oil by Govt.	Collection charges	Net cess collection	Payments made to OIDB under Section 16 of Act
		(Rs. in Crores)		
1991-92	2500.64	16.76	2483.88	95.00
1992-93	2207.61	14.70	2192.91	—
1993-94	2366.64	15.86	2350.78	—

16. Asked whether the OIDB funds were sufficient to meet the oil companies requirements, the Ministry stated in a note:—

> "In the past, it has been possible to meet the requirements of funds from the available resources. In view of greater thrust to the oil exploration and development efforts planned in the coming years, the requirement of funds will outstrip the availability with the OIDB. Therefore, there is an imperative need to supplement the OIDB's resources and towards this, to pass on to the OIDB larger share of the cess collected by the Central Govt. for the purpose of the development of oil industry."

During the course of evidence the Committee pointed out that out of total cess of Rs. 20,000 crores collected so far only Rs. 902 crores had been released, which is less than 5%. Asked whether the Ministry ever approached the Ministry of Finance to enhance the allocation for oil developmental schemes, the Petroleum Secretary stated:—

"We have done this repeatedly and the Finance Ministry is also represented in the Oil Industry Development Board. Even this year also we have asked additionally but nothing has been given. To control their Budget deficit they say they are unable to allocate more money under this. This has been the Finance Ministry's stand. In fact, we said normally it is meant for this, but because of the constraints, the full money is not coming to the OIDB."

17. On being pointed out by the Committee that the cess was meant only for development of the oil industry, the witness stated:—

"Parliament has passed it and as officials I do not think we should comment on this. They say whatever has been meant for this purpose has not been used. This point has been raised since it comes through as budgetary allocation approved by the Parliament. There are certain areas which go beyond this where Government feels that certain other developments should take place and the OIDB Funds are used as supplementary funds to assist the oil companies. But, unless we have matching infrastructural development with oil growth, we cannot follow our policy. OIDB gives loan to develop infrastructure. So it is used to supplement the total effort in development of oil industry."

18. On being further pointed out by the Committee whether the collection of cess was specifically for oil industry, the witness replied that technically there was nothing wrong in that.

19. However, the witness agreed to the suggestion of the Committee as a matter that of principle the entire amount of cess should be given for investment in the petroleum sector.

20. The Committee further pointed out that there was need for enhancing the indigenous crude oil production for whcih substantial funds were required for taking up new projects. Asked whether the enhanced allocation to OIDB would not help the oil industry in this regard, the Petroleum Secretary replied during evidence:—

"OIDB supplements the resources of oil companies so oil companies must have matching resources. When Planning Commission do this exercise, fix the plan, they take into account, the OIDB money going to which project, to which company. So as a principle, that no project of an oil company, if it is supported by its own should suffer for want of funds. Again, we are just now coming out of the past three-four years. We ran into very heavy deficit. The pool had not paid its dues to the oil companies. So there was a resource crunch and similarly foreign exchange was also not available. We are coming out of this. I agree with you that this should be the principle.

Secondly, we had come with an additional exploration plan where we had asked for additional money so that we could establish the

additional resources. Now we are urging that whatever is needed should be given and it would be greatly strengthened by the recommendation of this Committee. So money from OIDB should be made available to match the resources of oil companies."

Elaborating it further, he added:—

"As far as the schemes regarding the additional exploration are concerned, we did ask the Finance Ministry. It is on record. They have said that they will not be able to spare any money for this purpose. Therefore, we are going ahead with meeting those requirements, by going through the capital expenditure route. The Finance Ministry had already agreed to this."

(c) Cost of Imported Crude

21. The landed cost of imported crude is derived by adding Ocean freight landing charges etc. and 35% Customs duty to the purchase price either on term basis or spot tender basis as the case may be. Table given below shows the landed cost of imported crude and the prices of indigenous crude paid by the refineries during the last 4 years:—

Period	Imported crude (landed cost)	Rs./MT Indigenous crude
1989-90	3189.68	2269.12
1990-91	4447.15	2442.80
1991-92	4735.08	2442.80
1992-93	5137.83	
— Upto 15.09.92		2442.80
— w.e.f. 16.09.92		3002.48
1993-94	5145.61	3295.76

22. The Committee pointed out that indigenous crude oil was much cheeper than the imported crude oil and enquired about the schemes finalised to increase indigenous crude oil production. The Petroleum Secretary stated:—

"We have for the rest of the three years of plan, proposed an expenditure of about Rs. 5000 crores for intensive exploration to establish more resources so that the increased oil would come from 9th Plan onwards."

(d) Royalty

23. Royalty in respect of mineral oil is payable under the provisions of Section 6A of the Oilfields (Regulation and Development) Act, 1948 and the Petroleum and Natural Gas Rules, 1959. According to these provisions, rate of royalty shall not exceeds 20% of the sale price at the oilfields or the oil well head. The rate of royalty shall not be enhanced more than once during any period of three years. Government had revised

the rate of royalty for crude oil for the period 1.1.1990 to 31.3.1993 to Rs. 481/MT. For the year 1993-94, an 'on account' payment at the enhanced rate of Rs. 528/MT towards royalty on crude oil is being made subject to notification of the final rate of royalty and the finalisation of crude price in due course.

24. During the course of examination, the Committee pointed out that some of the States like Nagaland were complaining about the payment of royalty. Asked about the reasons there of the Petroleum Secretary replied:—

> "In the North-East, the only problem which is topical is about Nagaland. In so far as Nagaland is concerned, under the orders of the State Government, ONGC has been stopped from extracting oil. Some interpretation which they have taken is about how the ONGC should be the work. We have got this matter examined earlier, both with reference to the various laws as well as the Constitution. We have got the opinion of all."

He added:—

> "According to the legal opinion we have and as given by the Attorney General the interpretation of the Constitution, there is no way the State Government can stop ONGC from extracting oil. It seems the issue is more political than legal, though outside it is shown as legal. Anyway to sort out these political sensitivities we had asked the Ministry of Home Affairs to intervene. An informal meeting was arranged with the Chief Minister of Nagaland and our Minister for Petroleum and Natural Gas. In pursuance of this, they want ONGC to execute an agreement. In fact, we are constantly in touch with the State Government to give us a draft of the agreement which they wanted us to execute, so that we can examine and execute as it was done earlier within the framework of the law. So, we have been persuading with the State Governments locally and at the Ministry level and at the Home Ministry level. So far, ONGC has not been able to resume production, but we have been exerting persuation and pressure from the Home Ministry."

25. Asked whether other States were also agitating over the royalty issue, the witness replied in negative. He, however, added that the royalty rates were fixed on the basis of an expert Committee Report which consulted all the concerning States.

III. Refining Cost

26. The Refineries are compensated through retention price scheme. Under the scheme the refineries are compensated their operating costs plus

12% post tax return on networth. There are 13 Refineries engaged in processing of crude oil. The following statement shows company-wise locations of the refineries and their processing capacities:—

(In Million tonnes per annum)

(i)	Indian Oil Corpn. Ltd. Guwahati	0.85
(ii)	Indian Oil Corpn. Ltd. Barauni	3.30
(iii)	Indian Oil Corpn. Ltd. Koyali	9.50
(iv)	Indian Oil Corpn. Ltd. Haldia	2.75
(v)	Indian Oil Corpn. Ltd. Mathura	7.50
(vi)	Indian Oil Corpn. Ltd. Digboi (Assam Oil Division)	0.50
(vii)	Madras Refineries Ltd. Madras	6.50
(viii)	Cochin Refineries Ltd. Cochin	4.50
(ix)	Hindustan Petroleum Corpn. Ltd. Bombay	5.50
(x)	Hindustan Petroleum Corpn. Ltd. Visakh	4.50
(xi)	Bharat Petroleum Corpn. Ltd. Bombay	6.00
(xii)	Bongaigaon Refinery & Petro-Chemicals Ltd. Bongaigaon	1.35
(xiii)	Simple Crude Distillation Narimanem (Project under implementation) unit at Penengudi near Nagapettinam for processing of Cauvery Basin Crude	0.50

27. The overall capacity utilisation during the year 1991-92, 1992-93 and 1993-94 was 99.2% 103.1% and 101.9% respectively. The following table

shows the capacity utilisation and cost of production in respect of each refinery during the last 3 years:—

Statement Showing Refinery-wise performance during the period 1991-92 to 1993-94

	HPC-BOM	BPCL	CRL	MRL	HPC VIZAG	IOC HALDIA	IOC KOYALI	IOC MATHURA	IOC BARAUNI	IOC GUWAHATI	IOC DIGBOI	BRPL
CRUDE PROCESSED												
STANDARD THROUGH PUT (TMT)	5200	6000	4150	5100	3900	2500	9000	7100	3000	800	500	1000
ACTUAL ACHIEVED (%)												
1991-92	90.40%	115.83%	116.84%	108.43%	100.74%	121.48%	103.97%	106.00%	75.40%	107.75%	109.00%	116.20%
1992-93	112.35%	120.70%	124.29%	104.20%	116.28%	122.00%	108.32%	110.35%	76.23%	101.25%	109.20%	111.70%
1993-94	115.08%	120.12%	117.01%	112.06%	115.00%	124.52%	104.79%	120.17%	74.03%	107.63%	111.20%	120.00%
DISTILLATES												
STANDARD (TMT)	3494	4593	3315	3384	3063	1315	4738	4972	2369	607	314	750
ACTUAL ACHIEVED (%)												
1991-92	86.63%	121.90%	117.89%	111.08%	87.46%	125.70%	122.16%	118.44%	76.05%	115.16%	109.55%	119.60%
1992-93	105.61%	123.23%	123.56%	105.50%	95.95%	124.87%	129.61%	110.78%	77.53%	108.40%	107.64%	116.13%
1993-94	109.42%	121.36%	116.89%	113.77%	104.90%	125.93%	123.72%	121.30%	77.36%	118.45%	108.28%	128.40%
REFINING COST												
RS./MT	207.81	282.31	287.58	264.42	300.21	263.51	143.68	184.69	312.69	489.23	746.05	335.34

28. During the course of examination the Committee pointed out that the refining cost of some of the refineries like IOC-Guwahati, Digboi and BRPL was very high. Asked about its reasons, the Ministry of Petroleum & Natural Gas replied in a note as follows:—

> "The refineries are compensated under the pricing mechanism for the return on investment and operating expenses. It is not possible to straightaway compare the performance of various Indian Refineries, using any single standard parameter. Similarly, the return on investment per ton, and operating expenses per ton are also not comperable among the refineries. This is due to the fact that the refineries have got different infrastructural facilities, technologies, types of crude processed, and secondary processing facilities available. Similarly, the capital employed for various refineries inclusive of cost of net fixed assets and working capital vary from refinery to refinery based on the age of refinery, location, configuration and volumes handled".

29. On being pointed out that capacity utilisation of Digboi refinery was very low and consequently the cost was high a representative of the Ministry stated during evidence:—

> "Digboi is a very old refinery and there are a large number of small units. Their maintenance is very high".

30. Asked whether there was any modernisation/renovation programme a representative of the Ministry stated:—

> "As far as our refineries are concerned, modernisation project is under implementation. But so many things come in between like the happening in Kuwait and the prices went up. I can tell you that the project is on and we will complete it".

31. Explaining the position about Guwahati refinery, the witness stated:

> "It will be completed by next year. Guwahati refinery is the first refinery in the public sector. It was commissioned in 1962. It is now thirty two years old and it is a small capacity refinery. If you compare it with Gujarat and Mathura, it is less because their capacities are much higher. This is one of the factors".

32. The Committee further enquired about the steps taken by the refineries to reduce their operational costs. The Ministry in a written note stated:—

> "Cost of Petroleum products produced at refineries comprises of crude oil, processing costs and return on investment. The cost of crude alone constitutes about 94% of the product cost. Therefore, scope of reducing cost of pertroleum products is marginal. The retention prices of the individual refinery are fixed based on the cost of production. In order to exercise control over the cost of

production, the performance of the refineries are monitored by OCC on monthly basis to maximise capacity utilisation, optimising the product pattern and reducing energy consumption through control of fuel & loss. To reduce the energy consumption in the refineries Joint Energy Audit has been conducted. Because of these measures, fuel & loss percentage in the refineries have shown a downward trend from 6.6% in 1988-89 to 6% in 1992-93%.

33. The Ministry further informed in a written note that several cost control measures were being taken by the refineries in areas like saving in chemicals, catalysts, stores, overtime, travelling printing & stationary, communication, staff car and repairs and maintenance.

34. The Committee also wanted to know the cost of production of products processed in the Indian refineries *vis-a-vis* price of imported products. The Ministry replied in a note as follows:—

"Cost of production under the existing pricing mechanism varies from refinery to refinery depending on the capital employed, refining cost and volume of crude thruput. The international petroleum product prices are primarily determined on global supply-demand positions, international crude prices and other geo-political factors and keep changing even during short span of time. A comparative statement of domestic cost of production at refinery level of major imported products on a weighted average basis for the Indian refineries as compared to landed cost of improted product inclusive of customs duty is as under:—

Product	Estimated Cost of Prod. April' 94 (Rs./SU)	Landed Cost April' 94 (Rs./SU)
SKO	4200.63	4395.52
HSD	4371.60	5624.94
LPG	4850.87	8433.79

35. The Committee also wanted to know whether present system of 12% return on net worth was sufficient particularly when more resources were required for expansion modernisation programmes etc. The Ministry of Petroleum & Natural Gas in a written note stated:—

"In a competitive economy the return on investments is determined by the market forces as well as tariff regime and the investor can enhance their post tax earnings through efficient management of working capital, capacity utilisation and other management techniques. In a deregulated economy, the retention pricing will therefore be not expected to continue".

36. Elucidating it further, the Petroleum Secretary during the evidence stated:—

"Earlier this was on the capital employed. That concept, whole was changed by the Cabinet. It is fixed after taking into account what are the costs in this country and what should be reasonable return to induce anybody to make investment. It all depends upon the cost of the capital. As long as we are in the competitive environment, we can keep this fixed cost or reduce the captial costs. The expert opinion is that it should be reasonable to generate surplus resources".

Fuel Loss

37. Some quantity of crude oil is lost during processing at refinery. The small quantity is also used as fuel. For the purpose of standard through put of the refinery an allowance is made for these two factors on a normative

basis. The following statement shows the fuel loss percentage of various refineries during the last 3 years:—

	HPC-BOM	BPCL	CRL	MRL	HPC VIZAG	IOC HALDIA	IOC KOYALI	IOC MATHURA	IOC BARAUNI	IOC GUWAHATI	IOC DIGBOI	ERPL
STANDARD	6.00%	6.85%	5.76%	7.78%	6.49%	10.00%	5.97%	5.70%	8.47%	9.33%	14.60%	9.80
ACTUAL												
1991-92	5.64%	5.93%	6.21%	6.91%	6.44%	8.00%	5.13%	4.99%	8.93%	8.00%	13.03%	16.09%
1992-93	5.43%	6.17%	5.95%	7.28%	5.73%	7.87%	5.07%	5.17%	8.26%	7.53%	13.55%	15.67%
1993-94	5.33%	6.19%	5.99%	7.16%	6.29%	7.52%	6.46%	4.82%	7.65%	7.20%	13.13%	14.92%

38. The Oil Prices Committee Report (1976) stressed that refineries should take effective steps to bring down the incidence of refinery fuel and loss in view of the high cost of crude. The Committee also recommended that the Oil Co-ordination Committee (OCC) should also undertake a periodical review of the refinery fuel and loss percentage taking into account refinery's product pattern, throughput level changed in crude mix etc.

39. During the course of examination the Committee pointed out that there were different standard for fuel and loss percentage for different refineries ranging from 5.7% to as high as 14.6%. In the case of BRPL as against the standard percentage of fuel and loss of 9.80% the actual fuel and loss ranged between 16.09% to 14.92%. On being asked whether the Ministry of Petroleum & Natural Gas had fixed any norms for fuel and loss percentage for each refinery with particular reference to BRPL where the fuel and loss percentage was very high, the Ministry of Petroleum & Natural Gas stated in a written note as follows:

> "Percentage fuel and loss of the refineries vary depending on the complexities of the individual refinery depending on types of the products which have to be produced. A refinery producing lubricating oil and high percentage of diesel and kerosene require more fuel consumption due to further intensive secondary processing. Apart from that high capacity refinery is normally more efficient and, therefore, in a smaller refinery on percntage basis fuel and loss is higher. Keeping all the above aspects in view, fuel and loss percentage norm of each refinery is fixed time to time by the Ministry of Petroleum & Natural Gas and the same is called as "standard fuel and loss" for individual refinery".

40. As regards the reasons for high fuel and loss percentage in BRPL refinery the Ministry replied:

> "BRPL is a petroleum refinery-cum-petrolchemicals. The standard percentage fuel and loss of 9.8% of BRPL is only for the refinery part whereas the actual fuel and loss as reported between 14% to 16% includes the fuel and loss for the petrochemicals part also and hence the difference".

IV. Efficiency of Pipeline Network

41. One of the areas having a bearing on refining cost/prices of petroleum products is the efficiency of pipeline network laid for

transportation of crude oil and petroleum products. The existing crude oil/ petroleum products pipelines owned by oil companies are as under:—

A. A. *Crude Oil Pipelines*

Pipeline	Length of pipelines (KMs)	Installed Capacity (MMT)
ONGC		
Bombay High-Uran-Bombay	210	20.00
Western Sector	259	9.50
Eastern Sector	123	2.25
OIL		
Naharkatia-Digboi	36	0.55
Naharkatia-Moran	51	2.75
Moran-Jorhat	82	3.75
Moran-Jorhat-Gauhati	268	5.20
Gauhati-Bongaigaon	156	5.00
Bongaigaon-Barauni	601	3.30
IOC		
Salaya-Viramgam	275	10.00
Viramgam-Koyali	141	3.00
Viramgam-Mathura	803	7.00

B. *Product Pipelines*

Pipeline	Length of pipeline (KM)	Installed Capacity (MMT)
A. *IOC*		
(i) Koyali-Ahmedabad (KAPL)	116	1.10
(ii) Barauni-Kanpur (BKPL)	669	1.80
(iii) Gowahati-Siliguri (GSPL)	435	0.82
(iv) Haldia-Barauni (HBPL)	525	1.40
(v) Haldia-Mourigram-Rajbandh (HMRPL)	268	1.25
(vi) Mathura-Delhi-Ambala-Jallandhar (MJPL)		
(a) Mathura-Delhi	147	3.70
(b) Delhi-Ambala	202	2.20
(c) Ambala-Jallandhar	164	1.35
B. *HPC*		
Bombay-Pune Pipeline (BPPL)	161	2.00

42. There are separate pipelines for the transportation of crude oil and products. For the crude oil pipeline, the trasnportation cost is built up recognising 12% post tax on the average net worth at the beginning and close of the year as per the balance sheet and intrerest on adjusted borrowings (net fixed assets + 30 days) operating expenses less depreciation—net worth) at the weighted average interest rate for the company, and the operating expenses inclusive of depreciation to be claimed on moderated capacity of the pipeline or the capacity of the refineries receiving such crude oils as the case may be. In the case of product pipeline also the transportation cost is built up on similar lines and based on 80% capacity utilisation or as estimated. The volume of the products to be handled through the pipeline is that approved by the Government.

43. The following table shows the comparative data of inland/coastal movements of POL:—

Per 1000 KM

Product Movement	*MS*	*SKO*	*HSD*
Rail (Rs./KL)	823	498	907
Road (Rs./KL) (Ex-Bombay)	994	994	994
Pipeline (Rs./Ton-KM)	127	127	127
Coastal (Rs. MT)	130	130	130

Crude Movement	*Per 1000 KM.*
Pipeline (Rs. /Ton-KM)	91

44. During the course of examination the Committee pointed out that movement of petroleum products through pipelines was much cheaper. Asked about the efficiency of pipelines network of various oil companies, the Ministry of Petroleum & Natural Gas furnished the following data. The following table shows, the standard thruput and as obtained for various Crude/Product pipelines for the years 1991-92, 1992-93 and 1993-94:—

(Figures in MMT)

Unit	*Capacity*	*1991-92*	*1992-93 (%age utilisation)*	*1993-94*
A. Product				
GSPL	0.818	83.130	96.577	115.281
KAPL	1.100	115.727	122.273	136.818
BKPL	1.800	93.722	105.778	103.889
HBPL	1.400	99.143	108.643	101.643
HMR	1.250	131.040	126.320	127.760

1	2	3	4	5
MSPL	3.700	101.622	99.541	109.703
Sub. Total	10.068	103.556	107.489	113.200
DTPL(AOD)	0.485	92.990	95.052	96.289
Total (PPL)	10.553	103.070	106.917	112.423
B. CRUDE				
SMPL	10.000	116.280	123.340	122.560
G. Total	20.553	109.497	114.908	117.355

45. On being enquired about the reasons for low capacity utilisation of DTPL, a representative of the Ministry stated during evidence:—

> "In one or two cases in the last 3 years, transportation by pipeline was less because product was not available. Otherwise pipeline efficiency is there hundred percent."

Ocean Loss

46. When crude is transported by ocean tankers some loss is inevitable. In the case of imported crude oil this ocean loss represents the difference between the quantity loaded in the tankers at the load point i.e. Bill of Lading quantity and the quantity received in the shore tanks at the disports. The OPC 1976 laid down a uniform rate of ocean loss at 0.5% of the Bill Lading quantity. In case the refinery suffers Ocean loss less than the ceiling, the difference between the actual and ceiling may be retained by the refinery as an incentive to bring down the Ocean loss.

47. The following table shows the average ocean loss percentage from 1988-89 to 1994-95:—

Year	% wt. ocean loss
1988-89	0.394
1989-90	0.372
1990-91	0.398
1991-92	0.361
1992-93	0.340
1993-94	0.322
1994-95	0.304 (Target)

48. As regards the steps being taken by the oil companies to minimise the ocean loss and its present status, the Ministry in their written note informed the Committee that an Industry Committee, set up in 1987 under the convenorship of Joint Secretary (C&A), Ministry of P&NG closely monitor the ocean losses. The monthly ocean loss figures are closely reviewed by OCC & MOP&NG and corrective actions are taken.

49. The Committee comprising of the members from the Marketing Divisions of all oil companies are analysing the ocean losses on a voyage to voyage basis and each case of any unusually high losses is being investigated.

50. Additional precautions are also being taken by way of utilisation of new technologies in measurement of temperature, volume and density of the crude, sounding system of the ships. Elaborating the position further during the evidence the Petroleum Secretary added:—

> "From 1988-89 onwards, it has come down to 0.3 per cent, another system of crude to be carried by the ships of the Shipping Corporation of India. Under the present policy, we are obliged only to use SCI ships. We took up the issue of loss with the Ministry of Surface Transport and the SCI and the loss has been brought down by improving the systems. The effort is on. In fact, we are pressing the Government for changing that policy also so that the oil industry should not be tied up with one shipping company. The figure given here from 1988-89 onwards shows that from 0.394 per cent, it has come down to 0.322 per cent."

V. Marketing and Pricing Mechanism

51. Marketing of petroleum products is carried out by four oil companies viz., IOC, HPCL, BPCL and IBP. These oil companies have a vast network of petroleum products spread all over the country. Marketing oil companies are entitled for:—

(i) Ex-refinery price of the product payable to the refineries.

(ii) Installation/Distribution/Administration cost.

(iii) 12% post tax return on networth.

52. The petroleum products are divided into two broad categories *viz.* the price administered products and free trade products. The major products like MS, HSD, Kerosene, LPG, Furnace Oil, LSHS Naphtha, Bitumen and ATF etc. are under the price-administered category for which the ex-storage point prices are fixed by the Government. Other products like Lube Base Oil and Lubricants, Benzene, Toulene, Raw Petroleum Coke etc. are in the free trade category for which the oil companies are free to fix the selling price on market considerations. About 90% of total volume of the petroleum products fall under price-administrered category.

53. The pricing of petroleum products is based on the retention concept whereunder the oil producing companies, refineries, marketing and pipelines are provided returns based on certain pre-determined norms. Under this concept, a fixed level of profitability for oil companies is ensured subject to their achieving laid down capacity.

54. During the course of examination the Committee enquired about the policy of fixing consumer price of various petroleum products. The Ministry in a note stated:—

> "The administered pricing policy of petroleum products ensures that products used by vulnerable sections of society like kerosene are subsidised i.e., sold to the consumer at even below the cost of production. Similarly, to achieve inter-fuel substitution, namely, to wean away the kerosene user to LPG and users of forest fuel to kerosene, LPG is also being subsidised. Simialarly, fuel like Naphtha, LSHS and FO used for fertiliser production are also subsidised as extensive use of fertilisers by the farming community is required for the growth of the Indian economy. Similarly, fuels like petrol etc. are priced in such a manner so as to promote their economic and effecient use."

55. Explaining the pricing mechanism further, the Petroleum Secretary stated during evidence:—

> "The basis of the current pricing is derived from the oil prices report of 1976 which was also submitted. That is the basic framework for whatever pricing system we have today, of course with the modification that has been done from time to time. The Committee, at that time, wanted to ensure that the essential petroleum products are made available to the public 1) at affordable price, 2) that there are no supply bottlenecks, 3) that some of the products used by the weaker sections should be subsidised and 4) that the pricing should be so adopted that we should discourage the inessential use of certain products. Broadly these are the factors which should govern the pricing policy. Based on that, the Committee went into that. The principle or the method that is used on pricing of refineries or marketing companies is that all the refineries which are marketing companies which have an investment will be given a post-tax return of 12 per cent and they have laid down some norms for their operating expenditure. Similarly, they gave a return on investment for the marketing companies. On this basis the pricing principles were determined. So, in order to see that this is properly monitored and evaluated, the Oil Coordination Committee was entrusted with this job. They get all the return, etc. from the marketing companies; investments are scrutinised; their accounts are also seen; and the compensation mechanism works in that way. In order to achieve this, OCC established a series of accounts to take care of the crude oil pricing."

56. The following table shows the level of prices of petroleum products in some of the Countries vis-a-vis India:—

S. No.	Country	MS (Petrol)	HSDO	LDO	Kerosene (Rs./litre)	F.O	ATF	LPG (Domestic) (Rs./Kg)	Exchange rate used
	1	2	3	4	5	6	7	8	9
1.	India (New Delhi)	15.71	6.17	5.52	2.54	5.14	10.98	5.81	
2.	Argentina (B Aires)	24.40	8.62	NA	9.46	NA	7.66	12.01	1 US$=1.00$ Peso
3.	France (Paris)	31.05	20.88	NA	NA	NA	NA	6.92	Re 1=0.17 FF
4.	Germany (Bonn)	26.11	20.74	4.68	8.83	NA	NA	NA	Re 19.2=IDM
5.	Japan (Tokyo)	34.63	20.13	NA	16.87	8.99	NA	9.52	Re 1 = 3.725 Yen
6.	Malaysia (K Pur)	13.09	8.02	8.04	8.15	NA	NA	14.57	Re 1= 0.81 M Cents
7.	Myanmar (Yangoon)	22.04	14.46	NA	18.59	11.71	18.59	20.90	Re 1= 0.1139 Kyet
8.	New Zealand (Wellington)	16.11	9.45	NA	12.45	7.43	9.99	6.87	Re 17.54=1.00NZ$
9.	Pakistan (Islamabad)	13.13	6.12	4.84	6.00	3.05	NA	8.47	Re 1=1.00 Pak Rupee
10.	Thailand (Bangkok)	12.67	9.33	9.21	10.70	3.85	NA	11.33	Re 1=0.84 Baht
11.	Vietnam (Hanoi)	8.07	7.49	NA	8.07	4.32	10.84	NA	Re 1=347 Dong

57. On being pointed out by the Committee that prices of petroleum products were low in some countries as compared to the prevailing prices in our country the Petroleum Secretary stated:—

> "A comparison strictly would not be tenable in the sense that import parity is totally governed by the market conditions. Here, we have laid down a very reasonable amount of compensation. We have introduced another element of subsidising some of the products. We have to take care that these subsidies are also recovered out of the overall sales which we make so that there is no impact on the budget. There is no drawal from the exchequer. These considerations will not strictly bear a comparison with the import parity which is purely market-based.
>
> In most of the countries, they follow market-based mechanism subject to some concessions. For example, some countries, even though it is market-based, impose a particular type of levy. Some others create a fund. There are variations in it. Every body contributes to it and somebody takes care of it. It all depends upon the conditions under which these people have allowed investments to be made in those countries unlike in our country where based on our Industrial Policy Resolution, petroleum was exclusively reserved for the public sector.
>
> So, right from the beginning, oil production right up to the marketing was totally under an administered price regime. So, I am not aware of any such situation which could be an exact parallel to what we had."

58. Elaborating, the position further, the Petroleum Secretary stated during evidence:—

> "If you look at the whole range of products, kerosene, LPG and, to some extent, diesel, and even naphtha are priced much lower in this country probably than in other country. It is only in the case of petrol, etc. that it is relatively high priced. They ensure that petroleum is available to them because, in turn, it generates other industries. We should curb the use of products, like diesel and petrol. For two reasons earlier, we were heavily importing petrol. We were importing diesel. The whole idea was that this should reduce our strain on the balance of payments position. But now, the new concern has come about the pollution. The only way to ensure that crude is used efficiently and carefully is to see that petrol is high-priced. There is a subsidy of Rs. 4000-5000 crore on kerosene which is probably the lowest priced product in the country. This subsidy has to be covered from products which bear a higher price and which are used by relatively better sections. This as I see is basically the reason why certain products are priced higher than the prices generally obtaining in other countries. Here, we must also admit the fact that very essential

products such as fertilizers and kerosene are available at lower prices."

59. Asked whether it was not possible to keep the prices of petroleum products low, the Petroleum Secretary replied:—

"The reasons for this price rise do not lie with the Petroleum Ministry only. You will find that whatever be the price policy of any product should be that the product in the market should be economically priced. To the extent that a product is not economically priced it does not reach the market at the particular price. Taking petroleum specifically two years back there was a demand from all State Governments for increasing the royalty. Today Nagaland has stopped the production. We had a series of meetings at the highest level. We had not raised the price of crude oil paid to ONGC since 1981. Other States are also pressing for additional resources. We have arrived at an agreement, that in future every year the royalty will be paid as on the basis of the production, as a proportion of it.

Now every year, the royalty is going up. Therefore, these costs have to be borne. Secondly subsidy is also going up not because of quantum but the quantity consumed is increasing. Because of the demand, we increased the price of kerosene. On LPG subsidy is going up. So, there must be a way for meeting the subsidy part. The only principle adopted here is that people who can afford to pay have been asked to pay. In our country, rightly or wrongly, petrol is considered as a very elitist product. It has to be understand. I have been in this Ministry for long and whenever we increase the price of petroleum products, we increase the price of kerosene by 25 paisa or so. We increase the price of diesel by 10 paisa and the increase in the price of petrol will be say three times of kerosene.

Because, the oil prices were going up and the subsidies were increasing. Our subsidies come to about Rs. 7,000 to 8,000 crore each year. Each year as the consumption goes up, subsidy also goes up. If we keep it like that, then the increase will be very steep and will be unbearable. Oil prices are raising and is likely to go up to 20 dollars per barrel. If it continues to be so till December, we will be forced to increase the price. There is no doubt about it. It is not a secret."

60. The Committee further enquired about the quantum of subsidy being given on various petroleum products. The Ministry of P&NG in a written note submitted that the quantum of subsidy during the year 1993-94 was

estimated to be Rs. 6596 crores spread among the following products:—

Products	Subsidy (Rs./crores)
Kerosene (Domestic)	3773
LPG Packed (Domestic)	1261
Naphtha (F)	503
FO (F)	167
LSHS (F)	102
HSD	575
Bitumen	126
Paraffin-Wax	89

61. On being further asked whether operational costs of the oil companies could be reduced so that prices of oil products could be lowered, the Petroleum Secretary replied:

"Inflation effects the oil companies also. Their wage bills are going up and the costs of materials are going up. If they are able to do that, that would be reflected in the price. Theoretically, it is possible to reduce the prices, but the most that would happen is the price may not be increased. At least it would be held at a particular level. But if you look at the wage spiral that is taking place today, especially it is an international phenomenon, though it is a related issue. With the coming into a large number of private companies and the multinationals with their salary structure etc., a number of public sector people are leaving. In fact, any revision of the wage also make take this into account. The Deptt. of Company Affairs has been considering this that it would have an impact on the public sector. When this type of spiral takes place it will be very difficult to keep the prices under control, especially when they are asked to operate within those norms.

He further added:—

"The cost cutting method is the only way. If they perform well, they will get 12 per cent more, post-taxes whatever it is. Since they are private shareholders, since their shares will be treated in the stock exchange they will be under compulsion to perform better. If they perform better they must reduce costs. This is expected of the operation of the market forces. It is possible that prices may become more competitive."

62. Asked whether the Govt. was reviewing the level of manpower and expenditure thereon with reference to volume of work in the Oil Companies, the witness stated:—

"Basically what all managements have now done is they have stopped the recruitment so that they can come to some desirable norms, except in very essential areas of speciality. The Exit Policy has to be evolved for the Government as a while, including the public sector.

We have a scheme which is called 'Petroleum India International' under which we take a large number of people in an organised way from oil companies to do work abroad. They will not only have a chance of going abroad but will be coming back also.

People are saying that they can operate the new rigs with fifty persons less than the number with which they are operating now. In fact, we have told the Ministry also that only the existing people should be deployed and no new recruitments should be made. Everybody is conscious that because of the economy instructions, whenever high level posts are sanctioned they are subject to strict scrutiny."

63. On being pointed out that there was tendency of increasing the prices every now and then and at times just before the Budget, the Petroleum Secretary replied during evidence:—

"Sir, it has nothing to do with the Budget. If you look at the earlier days, you would find that price revisions had been made even in the months of June, July. Whenever we want to balance the pool, we must have some time for the Financial Year to realise that price increase. Suppose, we do it in Budget, we would not have any time. Therefore, in fact, the last revision was done in the month of June, even it had to be done much earlier."

64. In reply to a question about the timing of price revision, the witness stated:

"We do this exercise only when we see that pool is going into deficit".

VI. Parallel Marketing

65. With a view to augment the availability of petroleum products the import of petroleum products other than crude oil, ATF, MS, HSD, FPO and Bitumen have been decanalised. The private entrepreneures have been allowed to undertake import of these commodities and sell them in the domestic market through their own network at market determined prices. Under the Kerosene (Restriction of use and Fixation of Selling Price) Order 1993 and the LPG (Regulation of supply and distribution Order, 1993) the parallel marketeers are required to intimate their intention and capabilities to import, bottle, market, distribute or sale of such products before commencement of their activities.

66. When asked about the objective of having parallel marketing, particularly for LPG and Kerosene, the Petroleum Secretary stated:—

"Because of these difficulties (deficit pool A/c) and because of growing demands, the subsidies on some of the products are increasing. Since the pool will not be able to bear these subsidies any more, we thought that the relatively better sections of the people should be able to pay for these products at market prices. So, consistent with the reform process, private investment was allowed. We have got a lot of safeguards so far as kerosene is concerned".

67. The Committee pointed out that private entrepreneures under parallel marketing system were facing certain problems due to non-availability of sufficient port facilities to import the petroleum products. Asked about the remedial measures being taken by the Ministry to remove such problems of the private parties, the Petroleum Secretary observed:—

> "There are problems in the ports. We have asked for import facility and storage facility which must be made available to the private parties also. On this basis, a monthly chart in advance is written down and indicated to these people. But, a large number of investments are coming up for development of major ports as well as minor ports. Investments are being done. After that, this will be available both for the private and the public sector. We will continue to have our public distribution system and therefore, market intervention is always possible; we are meeting a larger share of the demand in the market through public distribution system."

68. The Committee further pointed out that there were large difference between the prices charged by public sector oil companies and private companies selling LPG and Kerosene and enquired whether there could some diversion of petroleum products from PSU's to private parties, the witness stated:—

> "As far as import of LPG is concerned, the facilities are totally with the oil companies that without affecting their imports or public distribution system and so on, it must be available to parallel marketeers. Therefore, two things can happen. Since oil companies want to maximise their sale because they have got growth, they have sales entitlement, they are very-very keen on preserving extra LPG. We will take care of your point. It is construed as diversion but actually it is not a diversion. It is a supply made to them as a service by the oil companies".

69. Asked whether PSU's will be able to compete with the private companies, the Ministry of Petroleum & Natural Gas replied in a note as follows:—

> "As the parallel marketeers get established and grow in the business, the Public Sector eventually will have to compete with them, based on the customer service and competitive princing. The public sector oil companies are gearing themselves up to meet this challenge by obtaining new technology, improving management and marketing practices and resorting to cost cutting measures".

PART II

RECOMMENDATIONS/CONCLUSIONS OF THE COMMITTEE

1. The first systematic attempt to regulate the prices of the petroleum products was based on the recommendations of the Damle Committee, 1961. This Committee recommended fixing of prices of petroleum products on import parity basis as the bulk of the crude oil and major petroleum products were being imported. Later on the Shantilal Shah Committee, 1969 did not favour import parity as a concept as indigenous crude oil production and refining capacity had become a considerable factor by that time. However, import parity had to be continued because of the commitments made to the foreign oil companies in the refining agreements under which they had set up the refineries in India. Thereafter Oil Prices Committee, 1976 recommended discontinuance of the import parity principle and recommended that the pricing of major petroleum products on the refinery point be based on domestic cost i.e. retention price concept by taking the delivery cost of the curde oil, the cost of the refining of crude oil and reasonable return on the capital employed. The existing system of pricing of petroleum products continues to be based on the recommendations of the Oil Prices Committee, 1976 as amended by the Oil Cost Review Committee, (1984) wherein the pricing of the petroleum products for the production, refining and marketing units is based on the retention price concept. Under this system, oil producing companies, refineries, marketing companies and the pipelines are compensated operating cost plus fixed return on their net worth. The Committee's recommendations/observations relating to pricing of petroleum products are set out in the succeeding paragraphs.

2. Oil and Natural Gas Corporation Ltd. (ONGC) and Oil India Ltd. (OIL) are two main public sector organisations under the administrative control of the Ministry of Petroleum & Natural Gas engaged in production of oil and gas. The Committee find that cost of production of crude oil in ONGC increased from Rs. 917 per tonne in 1991-92 to Rs. 1124 in 1993-94. Similarly in case of OIL it increased from Rs. 517 in 1991-92 to Rs. 781 in 1993-94. As regards the reasons for vast variations between the costs of two companies the Committee were informed that this was due to the fact that ONGC's production mainly comes from off-shore projects where the cost of production was high. On the other hand OIL's projects were on-shore where cost of production was less. The oil companies are reported to have taken various steps to cut-down the cost of crude oil production which *Inter-alia* include application of value engineering techniques, controlling over-head and semi-variable expenditure, use of latest technologies and

introduction of improved managerial techniques etc. in addition to increasing efficiency at all the levels. Since 94% of the cost of petroleum products ex-refinery constitute the cost of crude oil alone and ONGC and OIL get cost plus 15% return on capital employed, the Committee stress the need for concerted efforts by the oil producing companies to contain the increasing cost of production of crude oil. The Committee also urge upon the Govt. to constantly review the performance of both the oil companies and carry out periodic cost analysis with a view to reducing the cost of production of crude oil.

3. The Committee note that in addition to average cost of production of ONGC and OIL of Rs. 1741 per tonne cess is added @ Rs. 900 per tonne. The cess is collected under the provisions of the Oil Industry Development Act, 1974 which provides for collection of cess on production of crude oil and natural gas at a rate fixed by the Govt. from time to time. The proceeds of the cess levied under the Act are first credited to the Consolidated Fund of India and thereafter the Govt. provides funds to Oil Industry Development Board (OIDB) for the development of oil industry after deducting the collection charges. The Committee are constrained to observe that as against the huge amount to the extent of about Rs. 20,000 crores collected as cess since the enactment of OIDB Act, an amount of only Rs. 902 crores i.e. even less than 5% of the total collection has been released to the OIDB so far for giving loans/financial assistance to oil companies for the programmes connected with the exploration, production, refining and marketing of oil/petroleum products. The Committee are further distressed to note that no funds have been released to OIDB after 1991-92. It is regrettable that the large funds collected for a specified purpose have been utilised by Govt. to control their budget deficit considering the meagre allocation of funds to the OIDB. The Committee are constrained to observe that the objective of enactment of the OIDB Act for collecting the funds for development of oil industry has not been adhered to.

4. The Committee also find that even though the Oil industry has been facing resource constraints, the Finance Ministry did not increase the allocation of funds to OIDB. In this context the Petroleum Secretary pleaded before the Committee that in view of the financial constraints in oil sector there was imperative need to enhance OIDB allocations to plan and execute new projects relating to oil production/refining. He added that the entire amount of cess after deducting the collection and other charges should be given for investment in petroleum sector. The Committee do agree to the fact that for enhancing the crude oil production and taking up new projects relating thereto, substantial funds/additional resources are

required. Considering the present trend of consumption of petroleum products and to curtail huge foreign exchange out-go on imports, it is essential that concrete steps are taken to increase both production of crude oil and refining capacity to reduce the import bill on account of petroleum products, which was to the tune of Rs. 17000 crores per annum. This all the more make the case for higher allocations to OIDB out of the proceeds of the cess levied/collected under the Oil Industry Development Act, 1974 on production of the crude oil/gas. The Committee, therefore, recommend that as per the provisions of the Act, after deducting the collection charges etc. the cess collected should be made available in full to the designated authority *i.e.* OIDB for making these funds available to the oil companies for projects in the field of exploration, production, refining and marketing of oil and gas.

5. The Committee find that all along the cost of production of indigenous crude has been cheaper than the cost of imported crude. For instance as against the cost of production of Rs. 3296 per tonne of indigenous crude during the year 1993-94, the cost of imported crude worked out to Rs. 5145 per tonne during the same period. Presently the ratio of indigenous and imported crude oil is almost 50:50. Considering the wide difference between cost of indigenous crude oil and imported one there is a strong case for adopting an accelerated exploration strategy to enhance the indigenous crude oil production. The Committee accordingly reiterate the recommendation made in their 4th Report presented to Parliament in February, 1994 that Govt. should adopt result oriented strategy for accelerated exploration of all the basins with a view to locate and develop the new oil and gas reserves in a time bound programme. Needless to point out that apart from gaining self-sufficiency in petroleum products, the enhanced production of indigenous crude oil being cost effective as compared to imported crude will have a favourable impact on the prices of petroleum products in the country.

6. The Committee find that yet another major component included in the price of crude oil is the royalty payable to the oil producing States. The royalty 20% of well head price of oil is collected under the provisions of oil fields (Regulations and Development) Act, 1948 and the Petroleum and Natural gas Rules, 1959. Incidentally, it came to the notice of the Committee that Nagaland had some complaints over the payment of royalty by ONGC which had been asked to stop the oil production in the State. In this context the Petroleum Secretary informed the Committee that the rates of royalty were fixed on the basis of an Expert Committee Report which consulted all concerned States also. The rates were being revised after every three years. He also stated that the efforts to resolve the issue in Nagaland were being made at the Home Ministry level. Since the prolonged agitation may hamper the oil production targets, the Committee would like the Govt. to deal the matter at the highest level.

The Committee also suggest that the whole question of royalty payment should be reviewed expeditiously.

7. Under the retention price concept, the refineries are compensated their operating cost plus 12% post tax return on their networth. Presently there are 12 refineries with a refining capacity of 53.25 MMT per annum. In view of the growing demand of petroleum products in the country, the refining capacity is proposed to be increased to 111 MMT by the 2001-2002 A.D. through setting-up new refineries as aslo through expansion of existing refineries. The overall capacity utilisation of the refineries during the years 1991-92, 1992-93 and 1993-94 was 99%, 103%, and 102% respectively. However, from the refinery-wise capacity utilisation it is noticed that capacity utilisation in IOC—Barauni refinery was only 74-76% during these years. The Committee would like the Govt. to examine the reasons for such a low capacity utilisation in Barauni refinery. Necessary steps/ modernisation programmes should be taken to enhance its capacity utilisation.

8. The Committee find that there are wide variations between refining costs of various refineries. As against the refining cost of Rs. 144 per MT in IOC-Koyali and Rs. 185 per MT in IOC—Mathura, the refining cost of IOC—Guwahati and IOC—Digboi was Rs. 489 and Rs. 746 per MT respectively. Similarly the refining cost in BRPL was Rs. 335 per MT. The Committee were informed by the Ministry that due to different infrastructural facilities, technologies, the types of crude processed and secondary processing facilities, the performance of various refineries was not comparable. Similarly the capital employed for various refineries inclusive of cost of net fixed assets and working capital vary from refinery to refinery based on the age of refinery, location configuration and volumes handled. The representative of the Ministry informed the Committee that modernisation/renovation programmes of refineries which were under implementation, would maximise capacity utilisation and optimise the product pattern. The Committee urge that concerted efforts should also be made to expedite the completion on-going renovation/modernisation programmes. As regards the other steps taken by the refineries to curtail their operational costs, the Petroleum Secretary stated that since the cost of crude oil alone constituted about 99% of production cost, scope of reducing cost of petroleum products was marginal. However, to effect economy, the refineries are stated to have taken several cost control measures in areas like saving in chemicals, catalysts, stores, overtime, travelling, printing and stationary, communication, staff car and repairs and maintenance.

The Committee recommend that the administrative Ministry should monitor and periodically review the performance of refineries at periodic intervals and ascertain the results of oil companies economy measures so that the refining cost is kept to the absolute minimum.

9. Some quantity of crude oil is lost during processing at refinery. A small quantity is also used as fuel. For the purpose of standard through-put of the refinery, an allowance is made for these two factors on a normative basis. The Oil Prices Committee Report (1976) stressed that refineries should take effective steps to bring down the incidence of refinery fuel and loss in view of the high cost of crude oil. The OPC recommended that Oil Coordination Committee (OCC) should undertake a periodical review of the refinery fuel and loss percentage. An analysis of the past performance of the refineries for the years 1991-92, 1992-93 and 1993-94 indicate that the fuel and loss vary significantly from refinery to refinery and range from 5.7% to as high as 14.6%. In the case of BRPL as against the standard percentage of fuel and loss of 9.80%, the actual fuel and loss ranged between 16.09% to 14.92%. Similarly in case of CRL and IOC-Koyali the actual fuel and loss was more than the standard norms during 1993-94. In this context, the Petroleum Secretary apprised the Committee that a refinery producing lubricant oil and high percentage of diesel and kerosene require more fuel consumption due to other intensive secondary processing. Apart from that high capacity refinery is normally more efficient and therefore in a smaller refinery on percentage basis fuel and loss is higher. As regards the higher fuel and loss in BRPL, the witness explained that the standard percentage of fuel and loss of 9.8% was for the refinery part whereas the actual fuel and loss included the fuel and loss for petro-chemicals also and hence the difference. In view of the huge cost of crude oil, the Committee urge the Govt. to make concerted efforts to further reduce the fuel and loss percentage so as to bring it within the standard norms.

10. One of the areas having a bearing on refining cost/prices of petroleum products is the efficiency of pipe-lines network laid for transportation of crude oil and petroleum products. The analysis of data relating to onland/coastal movement of POL furnished by the Ministry reveals that the capacity utilisation of pipelines except Digboi-Tinsukhia Product Pipeline (DTPL) has been optimal. The low utilisation of DTPL has been attributed to the non-availability of the product. It also came out during the course of examination that the movement of petroleum products through pipelines was much cheaper than other modes of transportation. For instance as against the transportation cost of Rs. 127 per 1000 k.m. for HSD the transportation cost for the same product by road and rail was Rs. 994 and Rs. 907 respectively. It shows that if more and more petroleum products are transported through pipelines, the cost of production (in turn marketing cost) can be reduced considerably. The Committee therefore, urge upon the Govt./Oil Companies we chalk out expansion programme for the existing crude/product pipelines as also for the new pipelines for transportation of petroleum products in the country.

11. When crude is transported by ocean tankers some loss is inevitable. The OPC, 1976 laid down a uniform rate of ocean loss at 0.5% of the Bill Lading quantity (difference between the quantity loaded and the quantity received in the shore tanks of the disports). The loss beyond the prescribed

norm is not to be adjusted in the Oil Industry Pool Account. But savings, if any, in the ocean loss with reference to this norm is surrendered to the oil industry pool account. As is evident from the date furnished by the Ministry for the years 1988-89 to 1993-94 the oil companies have reduced the ocean loss from 0.39% in 1988-89 to the present level of 0.32%. The Ministry informed the Committee that a Industry Committee set up in 1987 under the Convenership of Joint Secretary (C&A) Ministry of Petroleum & Natural Gas closely monitors the ocean losses. The Oil Coordination Committee (OCC) & Ministry of Petroleum & Natural Gas also review the ocean loss figures on monthly basis. The Committee comprising the Members from the Marketing Divisions of all oil companies were also active in analysing the ocean loss on a voyage to voyage basis. The Ministry is also reported to have taken additional precautions by way of utilisation of new technologies is measurement of temperature, volume and density of the crude, sounding system of the ships etc. These companies have now set a target to achieve further saving by slicing it down to 0.30% in 1994-95. The Committee hope that with the application of latest technologies and concerted efforts made to reduce ocean loss, oil companies will be able to achieve the targets.

12. Like the refineries, oil companies *viz.* IOC, HPCL, BPCL and IBP also get operating cost plus 12% post tax on their networth for marketing the oil products. The Committee have not gone into the details of the level of marketing costs in these companies. However, taking note of the fact that these companies have vast network of their offices/establishments spread over the country, in Committee's view any economy in their operation costs will have its impact on consumer price for petroleum products. With the liberalisation policy of the Govt. where private/multinational companies would also compete with PSU's, the Committee would like to emphasise the need to improve the work culture and to reduce the avoidable expenditure in marketing of oil products. As agreed to by the Petroleum Secretary, strict watch may be kept on manpower requirements of the companies to keep the wage bill at the minimum.

13. All the petroleum products are divided into two broad categories *viz.* the price administered products and free trade products. The major products like MS, HSD, Keresene, LPG Furnace Oil, LSHS, Naptha, Bitumen, ATS etc. are under the price administered category for which the ex-storage point prices are fixed by the Govt. Other products like lube oil and lubricants, Benzene, Toulene, Raw Petroleum coke etc. are in the free trade category for which oil companies are free to fix the selling price on market consideration. About 90% of total volume of the petroleum products fall under price administered category. The pricing of petroleum products is based on the retention price concept whereunder the oil producing companies, refineries marketing and pipelines are compensated for their operating costs based on certain pre-determined norms. Under this concept a fixed level of profitability for oil companies is ensured subject to their achieving laid down capacity. During the evidence the Petroleum

Secretary apprised the Committee that the present pricing mechanism has been adopted to ensure that after allowing the reasonable returns to oil companies, the products used by the vulnerable section are subsidised while products like petrol whose consumption is to be reduced are priced higher. The Committee find that the subsidy element in some of the petroleum products like kerosene, LPG, Naptha, HSD etc. has a significant bearing on pricing of petroleum products. Out of total subsidy of Rs. 6596 crores given during the year 1992-93 on such products, the kerosene alone accounted for Rs. 3773 crores. In this context the Committee would like to reiterate the recommendation made in their 4th Report that the supply of kerosene oil through PDS system should be reviewed expeditiously and people having higher income should be excluded. In Committee's view this step will help the Govt. in providing help to needy people and may also result in curtailing subsidy on kerosene.

14. The Committee regret to note that the revision of prices of petroleum products takes place too often. The Petroleum Secretary informed the Committee during evidence that the revision depends upon position of pool acccount. In case pool accounts were likely to become deficit, some balancing act has to be initiated. The Committee feel that proper estimation should be done well in advance so that there is no need to revise the prices of petroleum products too frequently. The Committee accordingly recommend that any revision of prices should be done normally as part of the Budget.

15. With a view to augment the availabiliy of petroleum products the import of petroleum products other than crude oil, ATS, MS, HSD, FO and Bitumen have been decanalised. The private enterpreneures have been allowed to undertake import of these commodities and sell them in the domestic market through their own network at market determined prices. Under the Kerosene (Restriction on use and Fixation of Selling Price), Order 1993 and the LPG (Regulation of Supply and Distribution) Order 1993, the parallel marketeers are required to intimate their intention and capabilities to import, bottle, market, distribute or sale of such products before commencement of their activities. The Govt. does not play any role in the matter of fixing of prices on the petroleum products marketed by these companies. Explaining the objective behind decanalising only selected petroleum items, the Petroleum Secretary informed the Committee that subsidy element on products like (LPG and Kerosene) was fairly increasing and as such was straining the pool account. In order to fill the searing deficit, selected producets of mass consumption were de-controlled so that the section of the people who could pay for these products should bear the market prices. However, it came out during examination that parallel marketeers were facing certain problems due to non-availability of sufficient port facilities to import the petroleum products. In this context the Committee were informed that large investment was coming up for development of major ports as well as minor ports. After materialisation of

these schemes, the facilities would be available to the public sector as well as to parallel marketeers. The Committee would like the Government to expedite the completion of such projects so that objectives of introducing parallel marketing are achieved fully.

NEW DELHI;
November 7, 1994

Kartika 16, 1916 (Saka)

SRIBALLAV PANIGRAHI,
Chairman,
Standing Committee on
Petroleum & Chemicals.