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COMMENT

Uttam Gupta **asks why consumers should be fleeced for delayed decisions on projects leading to time and cost overruns**

Subsidising refinery costs

THE prices of all petroleum-oil-lubricant (POL) products (except kerosene) were raised by 15-30 per cent in July 1996. Since November end 1996, pressure for yet another hike has been building up. As in July 1996, the objective of the second hike — whenever it comes — would only be to reduce the burgeoning deficit in the Oil Pool Account (OPA).

As on April 1, 1996, the deficit was Rs 5,700 crore. This would have gone up to about Rs 11,700 crore as on 31.3.1997. The hike in prices w.e.f. July 3, 1996 was expected to yield a saving of Rs 9,700 crore. A little later, the hike in diesel price was restricted to 15 per cent against 30 per cent announced initially. Even after this, the savings would have been about Rs 7,700 crore. This would have left an uncovered gap of Rs 4,000 crore (Rs 11,700 less 7,700 crore) as on March 31, 1997.

At the end of November 1996, the Government revised the year-end deficit to Rs 15,500 crore and this is now estimated at a still higher level, Rs 18,000 crore. This is a whopping Rs 14,000 crore more than anticipated in July 1996. Not only the potential savings from the price hike i.e. Rs 7,700 crore have been fully neutralised, but there is also a further increase of Rs 6,300 crore.

The increase has been attributed to the depreciation of the rupee, rise in the dollar price of imported crude and increase in the quantum of crude/POL imports. Considering the magnitude involved as also the fact that the brunt of the corrective measures will fall on the public and all industries across the board, merely listing the factors is not enough.

Some aberrations are quite apparent. For instance, in regard to the price, with the bulk of the purchase by IOC being on a contract basis, the monthly variation in the price should not affect the outgo on such imports. Even in regard to spot purchases, the price of imported crude rose from $ 17 per barrel in July 1996 to $ 22 per barrel in early November 1996; thereafter, it declined. Clearly, purchases after November were at the lower price. Even during July-November, not all the purchases would have been negotiated at the highest price i.e. $ 22 per barrel. The price effect has thus been over-stated.

No doubt, the decline in domestic production of crude and higher demand for petroleum products exerted pressure on imports. However, these could not have been unknown in July, 1996. If the Government feels that these were unexpected, then, this is, to say the least, bad planning.

Unable to provide a convincing explanation, the Government has made a subtle attempt to under-state the extent of slippages after July 1996. At the end of November 1996, the July projection (post-hike) of year-end deficit was revised to Rs 9,700 crore. This made little sense. On this basis and the deficit without the hike being Rs 11,700 crore, the savings consequent to the price hike would work out to a meagre Rs 2,000 crore (Rs 11,700 less 9,700 crore). This flies in the face of the tall claim made then about the huge savings.

Moreover, if this much saving is all that is expected from a hefty increase of 15-30 per cent, how is the Government going to tackle a likely deficit of Rs 18,000 crore as on March 31, 1997? On this basis, it would need a price hike which is nine times the increase announced in July 1996, to be able to fully eliminate the deficit. For instance, petrol which is now selling for Rs 21 per litre will have to be hiked to about Rs 78 per litre.

Clearly, increase in the price of POL products does not provide a viable solution. The problem of deficit has to be tackled right at the source. At the outset, the Government should set the basic facts straight in regard to the quantum of deficit to instil confidence in the public.

As an immediate measure, the surplus taken away from the OPA at the beginning of 90s (about Rs 9,000 crore) should be returned to it to enable payment of outstandings to the oil companies. The surplus had accrued due to the low price of imported crude for a major part of the '80s and the low price allowed even on domestic crude. Now, when these factors have turned unfavourable, in all fairness, the funds should be returned. For the future, the Government should refrain from fiddling with the OPA.

A significant share of the cost of production of POL products is on account of various duties, mainly customs and excise. For instance, on imported crude, there is a 35 per cent customs duty, while POL imports attract duty at varying rates. On supplies of indigenous crude/POL products, there is excise duty. Additionally, on domestic crude royalty and cess have to be paid.

While giving revenues to the Government, these duties have a cascading effect on the production cost and, in turn, the deficit in the OPA or a higher price to the consumers. The increase in the C&F cost of crude/POL (due to increase in dollar price and rupee depreciation) and the quantum of imports have given a bonanza to the Government at the cost of DPA/users of POL products. Likewise, as and when the prices of POL were raised (July 1991, September 1992, February 1994 and July 1996), it gained by way of additional excise collection. Considering these gains, it will only be fair to reduce customs duty on crude/POL imports and excise duty on domestic supplies. The recent decision to hike the royalty on domestic crude should be reversed. The loss of revenue should be made up by increasing the overall tax collection through better compliance and preventing evasion.

Refinery projects are highly capital-intensive. A substantial portion of the investment cost is due to the escalation caused by delays in implementing projects. The observations in the report of the Parliamentary Standing Committee on Petroleum amply confirm this. Ironically, these inflated costs become the basis for deciding the extent of subsidy on products like LPG, kerosene, diesel and naphtha/fuel oil supplied to the fertiliser industry. It is, indeed, paradoxical that the users of these products, except kerosene, are being made to pay more and more by way of frequent hikes in prices and, yet, they are charged with being heavily subsidised.

Retention margins (RM) of refineries should be determined and paid on a normative basis. This would help in containing cost and, in turn, deficit in OPA. Instead of the Oil Coordination Committee (OCC), the task of managing the pool should be entrusted to an autonomous high-powered commission. Representatives of user industries and important consumer associations should be associated with the exercise to ensure transparency and accountability.

Domestic production of crude has been affected during the '90s due to the slow pace of exploration and development of oil fields. This is the result of lack of a clear-cut policy, lack of autonomy to PSUs and delay in taking decisions. Urgent reforms in these areas are needed to give a boost to production.

The proceeds from the cess on domestic crude which are estimated at about Rs 26,000 crore as on March 31, 1996, should be made available to the oil companies for implementing projects for exploration and development of oil fields, rehabilitation/renovation of existing fields, setting up of additional refinery capacity and distribution infrastructure. This will also be consistent with the objectives as laid down in the relevant Act.

There is need for managing the demand for POL through a rational energy policy. Presently, there is excessive use of fuel oil/LSHS and diesel in captive power plants/diesel sets. This can be avoided if the power situation is improved by speedy completion of new power projects, improving the plant load factor (PLF) of existing stations and reducing transmission and distribution (T&D) losses. The growing use of POL in the automobile sector, especially the private vehicle segment, needs to be checked. Promotion of a mass transport system can help a lot in this. This will be environment-friendly as well.

Energy conservation across the board i.e. industry, transport, agriculture and services etc., offers enormous potential for reducing the demand for POL. And yet, it is given lip-service only.

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