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The Oil Pool in deficit

The economy cannot absorb market-determined POL prices, says **Uttam Gupta**

THE Oil Pool Account, which had a accumulated surplus of about Rs 9,000 crore at the end of 80s and continued to remain in surplus in the early 90s, has a staggering deficit of Rs 3,800 crore at the end of 1994-95. It could be even more once the revised retention margins for oil companies are announced. Even as there is no credible explanation for this sudden reversal, the government's sole preoccupation now is to mobilise the sums needed to make necessary payments to the oil companies.

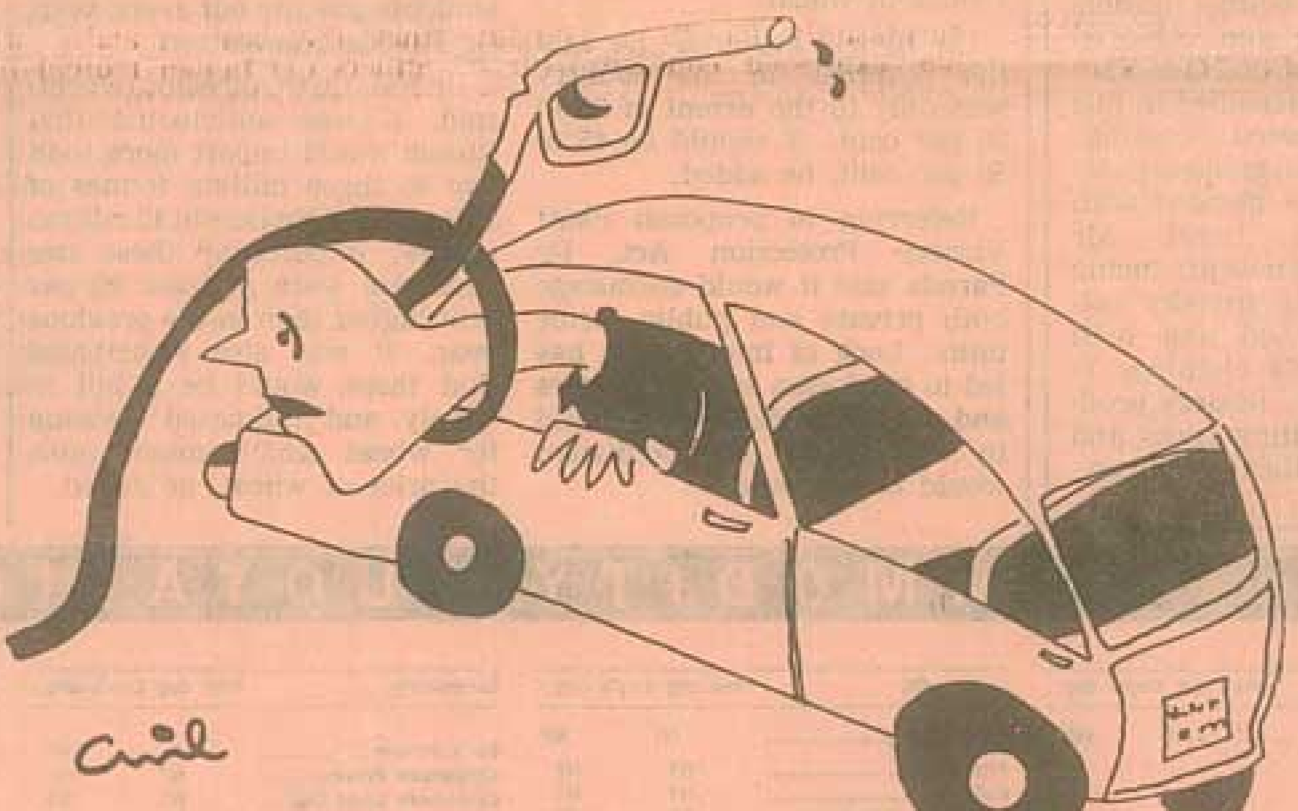
At the same time, it has made up its mind on abolishing the administered pricing mechanism (APM) for POL and introduce market-determined pricing mechanism (MDPM) albeit without examining the full implications from the view point of the user industries and consumers. What is, however, holding up the decision is the question of plugging the deficit in OPA.

So, while retaining the APM for the time being, the plan is to allow the oil companies to raise the selling prices of all presently subsidised items of mass consumption, i.e. diesel, kerosene, LPG and HSDO, to international levels. The resultant extra revenue would be more than sufficient to wipe out the deficit.

Such a decision is fraught with serious political consequences particularly in view of the impending general elections. Hence, the government proposes to subsidise the consumers directly through the budget. Since, under the proposed dispensation, the money will have to come from the exchequer, why not give the funds directly to the oil companies? Indeed, that is how it should be considering that in the past the government had no hesitation in appropriating the surplus in the OPA for meeting its own consumption needs. But, the government wants to highlight these as subsidy to the consumers and make them transparent. This way, it may also be preparing the ground for transition to a situation of no subsidy. An explicit allocation in the budget (like fertilisers or food subsidy) brings them under the concentrated focus of various watchdogs, including the IMF and World Bank.

How does the government propose to reach subsidised supplies to the consumers? An idea of this is available from the Sundarajan committee report. The contemplated mechanism envisages that the oil companies will charge the full price from the dealers. The dealers, in turn, are expected to sell to the consumer at prices which, it is presumed will continue to be notified by the government (as under the existing APM). The shortfall of this vis-a-vis the purchase price and dealers' commission will be reimbursed as subsidy. The Centre will provide necessary funds to the concerned state governments to facilitate this.

In short, the aim is to disburse a huge subsidy of about Rs 4,000 crore directly to millions through the wide dealer network besides involving the administrative set-up.



Do the state governments have the required infrastructure to handle, process, verify and dispose lakhs of claims? Considering that majority of states are financially squeezed, what is the guarantee that the funds allocated by Centre will not be misused? Even if there is no misuse/diversion, will the dealers be paid in time? Who will ensure that only genuine claims are entertained? Arising out of these is the real fear whether the consumers would, at all, get the products at subsidised price? Disruption in supplies and inter-state distortions will be additional problems.

This is not just theoretical and is amply borne out by experience in other sectors. For instance, in August 1991, the government had introduced the scheme of exempting small and marginal farmers from the 30 per cent increase in the selling price of all fertilisers. To facilitate this, a separate provision of about Rs 400 crore was made in Union Budget and the mechanism for administering this was similar to what is being contemplated in the context of the POL.

Under the scheme, while manufacturers were expected to transfer fertilisers to the distribution outlets for ultimate sale to farmers at the full price, the farmers were required to collect the discount from the concerned state authorities. The scheme was a fiasco and the government is on record having stated in the Parliament that only 5 per cent of a total of 65 million small and marginal farming families in the country benefitted.

Subsidy on food is another direct form of subsidy payment and its administration through the PDS has clearly exposed the inherent weaknesses, malpractices and misuse. The state governments have also been implementing direct subsidy schemes and their fate too is well known.

If this is the kind of subsidy mechanism the government is contemplating for POL, it would be much worse than having no subsidy at all. While the exchequer will be spending huge funds, these are unlikely to filter down to those for whom these are meant. Besides, it will impart a crippling blow to the process of deregulation and debureaucratisation even as, under the proposed scheme, endemic powers of the bureaucrats both in the state and Centre, get resuscitated with attendant serious consequences.

The present arrangement i.e. subsidisation of the POL through the OPA is the best. Ideally, the functioning of the OPA should be such that higher prices charged on products like petrol, ATV and motor spirit etc., fully pay for the subsidy on diesel, kerosene, LPG; as it was till a few years ago. Now, that there is a deficit for reasons best known to the government, let it pay the oil companies directly.

As regards market-based pricing, the key issue is whether the economy is ready to absorb steep increase in prices of essential mass consumption goods? The fact that the petroleum ministry is talking of soft landing in the context of its proposed 1996-2002 programme shows that it is not. That the ministry would put the necessary shock absorbers in place enabling switchover in 1998 is too good to believe. The problem is much too big to be taken care of by tariff changes or a few incentives.

And yet, if the green signal is given, say in 1998, while the oil companies will get away with high prices for all POL in view of their monopoly position; the rest of the economy will be at a serious loss. Even if the government decides to provide direct subsidy support through the budget, requisite funds may not be easy to come through. If the subsidy is discontinued, the results in terms of aggravation of inflation, further impoverishment of the poor and resultant closure of industries like fertilisers, will be mindboggling.

Instead of dismantling systems that have served as well in the past, we need to concentrate more on how these can serve us even better. In any scheme of reform while realistic pricing to consumers/users is no doubt important, there is need for check and scrutiny on oil companies as well to ensure that they bring down the cost of production and distribution. The government too needs to distance itself from the OPA and allow its functioning in an unfettered manner.