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Firing up oil & gas exploration (also see in Jpeg)

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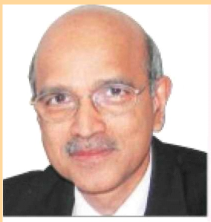
The government should extend the 80 IB tax benefit to all producing oil and natural gas blocks



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Over the last few months, the entire global energy landscape has changed drastically and we are now in the cusp of an inflexion point, from where the jury is divided over how the coming months and years play out. While one school believes crude oil prices—down by over half from last year's level—have bottomed out and if it stays at this level or drifts lower, future supplies will be severely threatened as large scale investments are being pulled back. Another school believes that days of high oil prices are permanently over and the world is awash with alternative and non-conventional sources like shale and tight oil, hitherto unviable, which will always act as a balancing power any time the prices threaten to rise unnaturally.

Whatever the outcome, India, which imports over 80 % of its oil demand, is currently in a sweet spot and will likely see its oil import bill down by over half from last year's level. This has provided a great opportunity to the government to put its finances in order by rationalising subsidies, without administering "bitter pills". India's oil & gas sector accounted for nearly 36% of India's total import bill in FY14 (versus nearly 31 % in FY10) while its contribution to overall exports also recorded a comparatively lower growth, at nearly 19 % (versus almost 17% in FY10). As per PPAC and finance ministry data, India's oil & gas sector contributed Rs3,05,350 crore in FY14, split almost equally between the central and state government as taxes and levies, making it one of the largest contributor to the exchequer. The sector contributed 15 % to India's total (direct indirect) tax revenue and 22.5 % to indirect taxes.

The government has already taken a bold step to completely deregulate the retail marketing of diesel, a process which began in January 2013 with the freeing of bulk diesel prices and raising retail diesel prices in small doses every month. Currently, retail prices of petrol and diesel are market-linked with consumers getting the benefit of lower crude oil prices. Government has also announced the introduction of nationwide direct benefit transfer (DBT) scheme for cooking gas, another bold step undertaken to rationalise subsidies.

Putting petro products under the ambit of GST would have been a major tax reform, but while they have been constitutionally brought under GST, they will not be subject to GST levy till notified. The current state and central taxes, like sales tax/VAT, CST and excise duty, will continue to be levied. We look to the gov-er nment to reduce CST to 1 % from 2 %, in line with the proposed Constitutional Amendment bill on GST, before eventually making it zero with bringing the petro products under GST. Refiners bear this burden which is neither reimbursed by the customer nor is recoverable nor canit be offset.

The industry wants the government to remove National Calamity Contingent Duty (NCCD) on crude oil levied at Rs51.5 per tonne, which was imposed on domestic and imported crude oil in the Budget FY04 for one year but continues to belevied till date, putting ad-ditional burden on the oil-refining companies. Alternatively, government may allow credit of NCCD for payment of excise duty/cess payable by oil companies on finished products. Refiners bear this tax even on exports of products using imported crude which should be exempted. Natural gas is a key feedstock in the refinery operations, and looking at the shortage of domestic gas, government should remove basic custom duty on imported natural gas. Currently the 5 % custom duty refiners pay is not recoverable in price of petroleum products under the RTP mechanism.

While the excise duty on branded fuel has been narrowed significantly with respect to unbranded fuel since last year, there still exists about ^1 per litre tax difference in petrol and about f 2 per litre in diesel. It is a well-known fact that premium fuel reduces consumption and enhances the life of the engine, thereby improving the overall efficiency hence there is a need to bring this at par urgently to promote branded fuel.

In a country which imports over 80 % of its crude oil requirements, the current policy—subjecting the services consumed by the E&P entities to service tax—drains away a substantial part of the funds committed for exploration, thus reducing the funds available for actual exploration activities. Crude oil/natural gas produced by E&P entities are not liable for excise duties, hence they cannot take CENVAT credit of service tax incurred for exploration and production of crude oil/natural gas. It is recommended that the government formulate a scheme forrefund of service taxpaidby E&P companies on the services consumed for exploration as well as production purposes. As an alternative, services provided to E&P companies which are essential for petroleum operations may be made "zero rated",sothatthereisnostrandingof taxes at the hands of service-providers.

In order to encourage self reliance in energy, the government should extend the 80 IB tax benefit to all producing oil and natural gas blocks and not just those assigned under NELP-VIII and CBM round IV

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