FIPI

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Dr. Hasmukh Adhia
Finance Secretary
Ministry of Finance, Department of Revenue
North Block, New Delhi - 110 001

Sub: OID Cess on Crude oil produced in India

Dear Sir,

It is a matter of great satisfaction and encouragement that the GOI has initiated a series of measures to attract investments and augment domestic production in the Oil & Gas sector. While some of the policies have already been put in place, many others are in advanced stages of formulation.

The industry welcomes these initiatives which will stimulate the Oil & Gas sector. However, as majority of the existing production comes from Nomination/ Pre-NELP fields, it is felt that there is a need to incentivize production augmentation from these fields in line with the new initiatives. Hon'ble Prime Minister of India has clearly laid out a vision to increase domestic production and reduce import dependence by 10% by 2022.

In this context, it is pertinent to point out one of the long standing demand of the industry has been to reduce the rate of Oil Industry Development (OID) Cess on Crude oil production. Despite having been raised at various platforms repeatedly, the demand of the industry remains unaddressed.

At 20% of the realized price of crude oil, the Cess continues to remain an overriding burden on the finances of the producing companies, leaving minimal surplus for reinvestments. There is an urgent need to reconsider the rate of OID Cess on crude oil in order to spur investment in the oil & gas sector.

In the above context, we are enclosing a self-contained note on the subject for your kind consideration. We wish to seek an appointment to present the case in person and shall be grateful if you could give us a time at your earliest convenience.

Thanking you,

Yours faithfully,

Dr. R.K. Malhotra
Director General

Encl. as above

cc. **Shri Kapil Dev Tripathi, Secretary, Ministry of Petroleum & Natural Gas, Shastri Bhawan, New Delhi**

Federation of Indian Petroleum Industry

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OID Cess on Crude oil produced in India

Historical Context

The OID Cess rate was increased from INR 2,500 per MT to INR 4,500 per MT in the 2012 Budget. While effecting the increase, the then Finance Minister clearly pointed out "Crude petroleum oil produced in India attracts a cess of INR 2,500 per metric tonne under the Oil Industries Development Act. This rate was last revised in Budget 2006-07. As a measure of indexation, I propose to increase the rate of cess to INR 4,500 per metric tonne." It may be recalled that the Crude oil prices were in the range of US$ 100/bbl in 2012. It was expected that with fall in Crude oil prices, the OID Cess rate would be commensurately reduced.

However, when Crude oil prices started falling below US$ 50/bbl, the industry requested for a reduced rate with the proposal to make the Cess rate ad-valorem in the range of 5 to 8% so that when the prices rise again, the GOI gets its share of higher revenue. It is pertinent to mention that, historically OID Cess has been levied in range of 8-10% of crude price (refer table below):

Year	FE Rate	Indian Basket		OID Cess rate		%: OID Cess to Crude price
	INR/USD	USD/ bbl	Rs./MT	Rs./MT	USD/ bbl	
2005-06	44.28	**55.72**	18,505	1,800	**5.42**	9.73%
2006-07*	45.25	**62.46**	21,197	2,500	**7.37**	11.79%
2007-08	40.26	**79.25**	23,929	2,500	**8.28**	10.45%
2008-09	45.91	**83.57**	28,774	2,500	**7.26**	8.69%
2009-10	47.42	**69.76**	24,811	2,500	**7.03**	10.08%
2010-11	45.28	**85.09**	28,897	2,500	**7.36**	8.65%
2011-12	47.95	**111.89**	40,238	2,500	**6.95**	6.21%
2012-13**	54.45	**107.97**	44,092	4,500	**11.02**	10.21%
2013-14	60.50	**105.52**	47,880	4,500	**9.92**	9.40%
2014-15	61.15	**84.16**	38,596	4,500	**9.81**	11.66%
2015-16 (upto Feb'16)	65.33	**47.08**	22,930	4,500	**9.19**	20.81%

*OID Cess increased to Rs. 2,500/MT w.e.f. 01.03.2006.

**OID Cess increased to Rs. 4,500/MT w.e.f. 17.03.2012.
BMT Factor of 7.5 bbl/MT is considered.

The Union Budget 2016 converted the Cess rate from specific to ad-valorem. However, it kept the ad-valorem Cess rate at 20% of the realized price of oil, which tantamount to keeping the Cess rate almost at the same rate of INR 4,500 per MT at the Crude oil price of around US$ 50/bbl.

High rate of Cess acts as a disincentive to incremental investments and production

Low oil prices together with high Cess ensured that Oil companies had minimal investible surplus. It acts as a disincentive to incremental production, investments and Enhanced Oil recoveries and Tight Oil & Gas projects.

OID Cess was earlier revised from Rs. 2,500/MT to Rs. 4,500/MT, when the price of Indian basket of crude was in the range of US$ 100-110/bbl. Under the revised rate of 20% ad valorem, even at half of that crude price levels, OID Cess works out at pre-revised rate of Rs. 4,500/MT.

Generating adequate investible surpluses is a necessary prelude to undertaking new investments to augment production.

Many governments the world over have reduced taxes (Government take) so that their Oil & Gas sector remain competitive, attract investments and support exploration & production activities

In these price regimes, governments have lowered their "take" to support higher exploration and production activities (please see table).

Country	Applicable to existing production?	Impact on Government Take	Measures
Indonesia	✓	Decrease	• Removed indirect taxes on exploration investment.
Angola	✓	Decrease	• Marginal terms legislated. Some PSCs renegotiated to increase cost recovery ceiling.
U.K.	✓	Decrease	• Supplementary charge rate decreased to 10%. • PRT rate reduced to 0% (effective 2016). • Extension of investment and cluster allowances to include tariff income.
Mexico	✓	Decrease	• Improved cost recovery terms for PEMEX assets.
Uzbekistan	✓	Decrease	• Kandim-Khauzak-Shadi PSC profit share renegotiated to improve investor IRR.
Ukraine	✓	Decrease	• Oil royalty rates reduced.
Source: *Petroleum fiscal systems: 2016 in review*, Wood Mackenzie, January 2017			

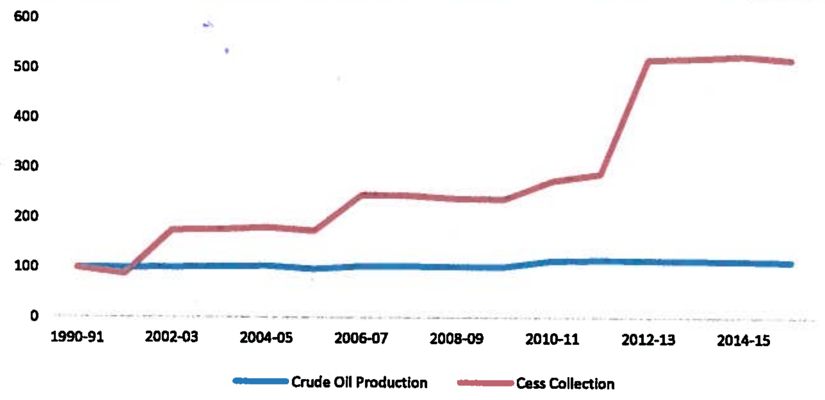
It is important to point out that just like in India, the U.K. government also increased its supplementary charge from 20% to 32% in the high oil price regime. However, when the oil prices started to fall, the U.K. government swiftly responded by reducing the Supplementary charge from 32 % to 10%.

India is one of the largest net importer of Oil. High taxes on domestic crude oil production undermines efforts to increase production

It is also pertinent to mention that OID Cess is not applicable on oil being produced/to be produced from NELP Blocks. OID Cess is also not payable under Marginal Field Policy and HELP notified by Government on 14 Oct'15 and 30 Mar'16 respectively. It is understood that these incentives have been extended under relevant schemes to augment domestic oil production. However, as brought out above, since, majority of the existing production comes from Nomination/ Pre-NELP fields, there is also a need to review the existing rate of 20% OID Cess.

It is pertinent to point out that even as oil production has increased marginally over the last 25 years, Cess collection from this production has grown significantly (please see chart). Imposing ever-increasing Cess on production has acted as a disincentive to production and incremental investments.

Crude oil production & Cess collection



1990-91 = 100. Production data from MoPNG Petroleum & Natural Gas Statistics & Annual Report. Cess collection data from OIDB Annual Report 2015-16

Recommendation

To conclude FIPI believes that reducing the Cess rate to a reasonable level of 8 % of the realized price of crude oil is an absolute necessity for the producing companies in the current price and cost environment.

While lower Cess rate will entail loss of revenue for the GOI, lower production tax shall spur investments leading to additional production and overall increase in taxes to the government in the form of Royalty, Profit Petroleum & Corporate taxes.