CHAPTER-6

DISINVESTMENT

OF

OIL SECTOR
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The National Common Minimum Programme, envisages that profit-making companies will not generally be privatised. All privatizations will be considered on a transparent and consultative case-by-case basis. The existing “navaratna” companies would be retained in the public sector while these companies can raise resources from the capital market. It also envisages that the public sector companies and nationalized banks will be encouraged to enter the capital market to raise resources and offer new investment avenues to retail investors.

In pursuance of the above policy the Government of India has set up a “National Investment Fund” and has also approved in principle the approach that

- currently unlisted profitable PSUs with net worth in excess of Rs. 200 crore could be listed through an Initial Public Offering (IPO), either in conjunction with fresh equity issue of the PSU or independently, on a case by case basis, subject to Government's retaining the residual equity of 51% and management control;

- sale of minority shareholding profitable PSUs either in conjunction with a public issue of fresh equity of the PSU or independently, subject to Government’s retaining the residual equity of 51% and management control.
**CAPITAL STRUCTURE OF OIL PSUs AS ON 31.3.2005**

(Rs. Crores)

<table>
<thead>
<tr>
<th>S.NO</th>
<th>PSU of the company</th>
<th>Authorised Capital</th>
<th>Paid up Capital</th>
<th>Govt. of India Holding in %</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>ONGC</td>
<td>1500.00</td>
<td>1425.93</td>
<td>74.14</td>
</tr>
<tr>
<td>2.</td>
<td>OVL</td>
<td>500.00</td>
<td>300.00</td>
<td>NIL</td>
</tr>
<tr>
<td>3.</td>
<td>OIL</td>
<td>250.00</td>
<td>214.00</td>
<td>98.13</td>
</tr>
<tr>
<td>4.</td>
<td>GAIL</td>
<td>1000.00</td>
<td>846.00</td>
<td>57.34</td>
</tr>
<tr>
<td>5.</td>
<td>IOC</td>
<td>2500.00</td>
<td>1168.01</td>
<td>82.03</td>
</tr>
<tr>
<td>6.</td>
<td>HPCL</td>
<td>350.00</td>
<td>339.00</td>
<td>51.01</td>
</tr>
<tr>
<td>7.</td>
<td>BPCL</td>
<td>300.00</td>
<td>300.00</td>
<td>66.20</td>
</tr>
<tr>
<td>8.</td>
<td>IBP</td>
<td>100.00</td>
<td>22.15</td>
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</tr>
<tr>
<td>9.</td>
<td>EIL</td>
<td>100.00</td>
<td>56.16</td>
<td>90.40</td>
</tr>
<tr>
<td>10.</td>
<td>BRPL</td>
<td>200.00</td>
<td>199.82</td>
<td>NIL</td>
</tr>
<tr>
<td>11.</td>
<td>KRL</td>
<td>150.00</td>
<td>138.47</td>
<td>NIL</td>
</tr>
<tr>
<td>12.</td>
<td>NRL</td>
<td>1000.00</td>
<td>735.63</td>
<td>NIL</td>
</tr>
<tr>
<td>13.</td>
<td>CPCL</td>
<td>400.00</td>
<td>400.00</td>
<td>NIL</td>
</tr>
<tr>
<td>14.</td>
<td>BALMER LAWRIE</td>
<td>30.00</td>
<td>16.29</td>
<td>NIL</td>
</tr>
<tr>
<td>15.</td>
<td>BIECCO LAWRIE</td>
<td>50.00</td>
<td>42.00</td>
<td>57.37$</td>
</tr>
<tr>
<td>16.</td>
<td>MRPL</td>
<td>2000.00</td>
<td>1762.00</td>
<td>NIL</td>
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</tbody>
</table>

In case of IOC and CPCL figures pertain to 2003-04 and the same for 2004-05 are yet to be finalised.
### FINANCIAL PERFORMANCE OF OIL PSUs DURING 2004-2005

<table>
<thead>
<tr>
<th>S.NO.</th>
<th>Name of the PSU</th>
<th>Gross Turnover (Rs.Crores)</th>
<th>Profit After Tax (Rs.Crores)</th>
<th>Dividend in %</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>ONGC</td>
<td>45826.00</td>
<td>12168.00</td>
<td>12168.00</td>
</tr>
<tr>
<td>2.</td>
<td>OVL</td>
<td>4768.60</td>
<td>981.87</td>
<td>NIL</td>
</tr>
<tr>
<td>3.</td>
<td>OIL</td>
<td>4517.65</td>
<td>946.36</td>
<td>33.92</td>
</tr>
<tr>
<td>4.</td>
<td>GAIL</td>
<td>12435.00</td>
<td>1947.00</td>
<td>17.36</td>
</tr>
<tr>
<td>5.</td>
<td>IOC</td>
<td>130202.95</td>
<td>7004.82</td>
<td>35.02</td>
</tr>
<tr>
<td>6.</td>
<td>HPCL</td>
<td>63000.00</td>
<td>1025.00</td>
<td>18.72</td>
</tr>
<tr>
<td>7.</td>
<td>BPCL</td>
<td>63125.61</td>
<td>721.02</td>
<td>30.00</td>
</tr>
<tr>
<td>8.</td>
<td>IBP</td>
<td>13620.00</td>
<td>13620.00</td>
<td>NIL</td>
</tr>
<tr>
<td>9.</td>
<td>EIL</td>
<td>900.00</td>
<td>96.00</td>
<td>44.21</td>
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<tr>
<td>10.</td>
<td>BRPL</td>
<td>32320.34</td>
<td>426.75</td>
<td>60.00</td>
</tr>
<tr>
<td>11.</td>
<td>KRL</td>
<td>13134.50</td>
<td>842.12</td>
<td>3.78</td>
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<tr>
<td>12.</td>
<td>NRL</td>
<td>4298.99</td>
<td>409.15</td>
<td>30.57</td>
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<tr>
<td>13.</td>
<td>CPCL</td>
<td>9430.45</td>
<td>400.05</td>
<td>18.61</td>
</tr>
<tr>
<td>14.</td>
<td>BALMER LAWRIE</td>
<td>1071.05</td>
<td>29.64</td>
<td>30.00</td>
</tr>
<tr>
<td>15.</td>
<td>BIECCO LAWRIE</td>
<td>40.71</td>
<td>0.93</td>
<td>NIL</td>
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<tr>
<td>16.</td>
<td>MRPL</td>
<td>20693.00</td>
<td>879.00</td>
<td>NIL</td>
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In case of IOC and CPCL figures pertain to 2003-2004 and the same for 2004-05 are yet to be finalised.

$ Equity held by OIDB
Though the imbroglio over the strategic sale of BPCL/HPCL is far from over, the mandarins within the governments have come up with yet another proposal to meet the year’s disinvestment targets. A booming stock market has inspired the bureaucrats in Delhi to suggest the sale of equity cross-holding the three top notch energy companies, IOC, GAIL & ONGC, hold in each via the book building route. The three energy majors, following a government diktat, had collectively spent Rs. 4,643 crores in January 1999, buying shares in each other. The move, widely criticised then, had helped shore up taking for a government facing revenue shortfall. Peculation was also rife that the government was in the process of a crating an integrated Indian energy behemoth to take under global energy giant post deregulation. While the governments intents, if it has any, regarding the structure of the energy industry is still hot air the current cell off is bound to generate another wind fall for the government.

For starter, IOC currently holds a 9.6 % stock in ONGC and another 4.5 % in GAIL “ONGC hold another 9.1 % in IOC and 4.8 % in GAIL while GAIL has 2.4 % stock in ONGC. Given the current bull run on the stock s the sale of these cross holdings is excepted to fetch around Rs. 174.5 billion from the market netting IOC nearly Rs. .75 billion, ONGC Rs. 34.4 billion and GAIL Rs. 17.6 billion with the government pocketing nearly Rs. 13 billion by way of capital gains. Deny , as some may, the unexpected wind fall is bound to reflect on the government ‘s balance sheet , this time facing a mounting deficit Per say , the divesture of cross holding makes perfects sense. The three energy giant have curved out aggressive growth strategies and are in the need for funds. Given the market run , there stock touching and all time high and the original purpose of cross holdings achieved , bailed out a government then facing review short fall, it would be in the scheme things to sell of there stakes to pursue greener pastures. What , how ever, is worrisome is a system and institution to decide the feasibility of excising what is essentially a business option and the intent of such moves in a sector so crucial to the overall health of the economy.
Given the current state of the economy with forex reserve touching a high of $100 billion the proposed sale has not generated much heat. However, the concerned this time round is the effect the proposed mop-up operations will have on the liquidity in the market just at a time when domestic retail investor sentiment are picking up and the effect it will have on the markets appetite for other government off loading in companies CMC and VSNL. More importantly, will the off loading provide the government the opportunity to privatize BPCL/HPCL throw the backdoor option? again, what happiness to the proceeds from this investment the windfall must been seen as one, which just shouldn’t end up being the feed tiding over current government expenditure. The ministry may well deny any direct linkage between the markets for the cross holding and these other scrip’s but it brings us back to the basic questions. When and how, if at all, does the government purpose to free the oil firms from the clutches of state control? The need for an integrated petroleum sector regulator has been touched upon by the in an earlier analysis (the quandary of oil sector reforms, ORF strategic trends, issue three, October 10 2003) and the present context only reinforces it. Now, even the power ministry has gone on record asking for a petroleum sector regulator. At the very least, a downstream regulator on the lines of the DGH (Directorate General of Hydrocarbons) is a pressing requirement if there blue chip public sector energy companies are to hold out in a deregulated environment.

**Indian Public sector disinvestment**

The Government of India is selling its holdings in the companies promoted by it. These companies, known as public sector companies, were promoted by the government for economic development and social justice. Theoretically, the intentions of setting up these companies were good. In practice most of these companies became a drag on the exchequer. Even though these companies enjoyed monopolies in their respective fields, the financial position of the majority of these companies are far from satisfactory. Inefficiency and corruption are common and they owe their existence to the directionless...
economic policies followed by the congress governments. The late eighties saw a changes in economic polices and this was immediately reflected in government policy regarding the public sector units. The policy makers felt that there was no point in supporting public sector units that are counterproductive to the economic growth of the country.

It was also felt that government funds in these companies by way of share capital can be better utilized if taken out. This formed the basis of the public sector disinvestment programs. It is also true that the present government is going blindly on the disinvestment program just to bridge the budgetary gap. The annual budget presented by the finance minister includes income from disinvestment. The actual funds generated from disinvestment invariably falls behind the government targets. There are many who want to take maximum benefit of the disinvestment process. Take the case of SEBI (Securities and Exchange Board of India. It advises the government on the need for PSU disinvestment in the local market as compared to overseas markets. This would boost the primary market and also stop the ownership of these blue chips from being transferred abroad. The regulator does not favour selling PSU stocks through the GDR route at the expense of the domestic market. "There is no problem of demand in the domestic market for the top ten PSUs," sources in Sebi said.

It is the government's view that a portion of divestment should be earmarked for the small investor. Some even believe in a capital market revival on the basis of the return of the small investor. The thinking within government is that since only institutional investors partake in the private placement market, it would be a good means of ascertaining the "right price." The present government is presenting a very optimistic picture. The disinvestment target was pegged at Rs 5,000 crore (Rs 100 crore = Rs 1 billion). Government sources now say that disinvestment may net Rs 6,000 crore (Rs 100 crore = Rs 1 billion) just from the sale of equity in four PSUs - Indian Oil, Gas Authority of India Ltd, Videsh
Sanchar Nigam Ltd and Container Corporation of India Ltd - for which cabinet clearance has already been obtained and the lead managers too are in place.

Privatization Of The Oil Sector

With each passing day economies are becoming much more complex and competitive. To progress in such times, indeed newer techniques have to be evolved; however one should be mindful of the old adage which says that, "the art of progress is to preserve order amid change and to preserve change amid order". Over the years the public sector has played a central role in enabling our country to accomplish the national objective of self-reliance. It is therefore natural to feel uncanny about the idea of disinvestment, specifically, when the issue is one of disinvesting a fortune 500 company. Supporters of the idea claim that to survive in an ever-changing economic environment, and for the economic progress of the nation, disinvestment is the key. It is therefore suggested that Industries which have become a liability for the government or in other words, which have not been running as well as they potentially should, may be disinvested.

Scenario Prior To 1990's

As India got Independence in 1947, a need was felt to build a strong nation, with a government that was attentive to the needs of its people, which would work for their betterment and prosperity. It was hoped that a strong government would own undertakings that would create employment, and work towards the eradication of poverty amongst other problems. The decades between independence and the 90' witnessed enormous industrialization, where the government set up companies, and built a strong infrastructure.

Post 1990's

By the advent of the 1990's, the Government had stretched its hands in almost every sector, be it iron and steel, agriculture, telecommunications, and
automobiles, while many of these government undertakings were doing well in their respective areas, few others were not getting the desired results.

The notion of disinvestment was first brought up in the year 1991, when the government, outlined the objectives of disinvestment as follows:

- It would broaden the equity
- Improve management
- Enhance the availability of resources for these enterprises
- Generate income for the exchequer

While initially, the idea was to disinvest not more than 20% of the government equity in selected public sector undertakings, a major transformation happened in 1996. The broad aspects of the policy of disinvestment as laid down at this time were:

- To classify the public sector non-core strategic areas for the purpose of disinvestment;
- To set up a Disinvestment Commission to deal with disinvestment related matters;
- To take and implement decisions to disinvest in a transparent manner;
- To assure the workers and employees of job security or, in the alternative, opportunities for retraining and redeployment.

The next important step was taken in 1999 when the government classified, public sector into strategic and non-strategic areas. Following were included in the list of Strategic Public Sector Enterprises:

- Arms and ammunitions and the allied items of defence equipment, defence air-crafts and warships;
• Atomic energy (except in the areas related to the generation of nuclear power and applications of radiation and radio-isotopes to agriculture, medicine and non-strategic industries);

• Railway transport.

All other Public Sector Enterprises were to be considered non-strategic. While initially the government proposed disinvestment of up to 26%-50% stake, over the years the policy of the government has undergone a huge change. At the present day the government is considering the idea of giving up its entire stake in the non-strategic areas where the establishments are running in losses. Because of the current revenue expenditure on items such as interest payments, wages and salaries of government employees and subsidiaries, the Indian government is left with hardly any surplus for capital expenditure on social and physical infrastructure. While the government should be spending on basic Education, primary health and family welfare, huge amounts of resources are blocked in several non-strategic sectors such as hotels, trading, consultancies, textiles, chemicals and pharmaceuticals, consumer goods companies etc. The continued existence of the PSUs (Public Sector Undertakings) is forcing the government to commit further resources for the sustenance of many non-viable PSUs. The government continues to expose the taxpayers’ money to risk, which it can readily avoid.

To top it all, there is a huge amount of debt overhang, which needs to be serviced and reduced before money is available to invest in the infrastructure. This makes disinvestment of the government stakes in the PSUs absolutely imperative. In its official web site (http://divest.nic.in/rationale.htm), the Ministry of Disinvestment, Government of India, has listed its primary objectives for privatizing the PSUs as follows.

• Releasing the large amount of public resources locked up in non-strategic PSEs, for redeployment in areas that are much higher on the
social priority, such as basic health, family welfare, primary education and social and essential infrastructure;

- Stemming further outflow of these scarce public resources to sustain the unviable non-strategic PSEs;

- Reducing the public debt that is threatening to assume unmanageable proportions;

- Transferring the commercial risk, to which the taxpayers' money locked up in the public sector is exposed, to the private sector wherever the private sector is willing and able to step in the money that is deployed in the PSEs is really public money and is exposed to an entirely avoidable and needless risk, in most cases;

- Releasing other tangible and intangible resources, such as large manpower currently locked up in managing the PSEs, and their time and energy, for redeployment in high priority social sectors that are short of such resources.

It also speaks of the other benefits

- Disinvestment would expose the privatized companies to market discipline, thereby forcing them to become more efficient and survive on their own financial and economic strength or cease. They would be able to respond to the market forces much faster and cater to their business needs in a more professional manner. It would also facilitate in freeing the PSEs from the Government control and introduction of corporate governance in the privatized companies.

- Disinvestment would result in wider distribution of wealth through offering of shares of privatized companies to small investors and employees.

- Disinvestment would have a beneficial effect on the capital market; the increase in floating stock would give the market more depth and liquidity,
give investors easier exit options, help in establishing more accurate benchmarks for valuation, pricing, and facilitate raising of funds by the privatised companies for their projects or expansion, in future.

Opening up the public sector to appropriate private investment would increase economic activity and have an overall beneficial effect on the economy, employment and tax revenues in the medium to long term. In September 2000, the Indian government approved the restructuring of the oil sector wherein it announced its decision that all stand-alone refineries would now be converted into subsidiaries of industry giants. This meant that all the small refining companies would then be merged into the bigger entities, thus streamlining the entire industry. The government approved the proposal to restructure four stand-alone refineries: CPCL (Chennai Petroleum Corporation Ltd), KRL (Kochi Refineries Ltd), BRPL (Bongaigaon Refineries and Petrochemicals Ltd), and NRL (Numaligarh Refineries Ltd). Under the re-structuring plan, CPCL and BRPL were to become subsidiaries of the IOC (Indian Oil Corporation) Ltd, while NRL and KRL would be the subsidiaries of the BPCL (Bharat Petroleum Corporation Ltd).

The process of restructuring was to be completed by the end of 2000 (that it was not, is another story). This move was expected to provide market access to stand-alone refineries on a continuing basis in the ensuing dis-mantling of the APM (administered pricing mechanism) which is expected to be com-pleted by April 2002. Right now, the government sets the prices for four petroleum products under the APM, but this control will no longer be with it in a years' time. In January 2001, the Hon'ble Minister for Oil and Natural Gas, Mr Ram Naik, declared that disinvestment in oil sector PSUs would be decided on a case-by-case basis instead of any blanket sell off. The Petroleum and Natural Gas Minister was responding to Finance Minister, Mr Yashwant Sinha's announcement in New Delhi that the Government will bring down its equity in 12 oil sector PSUs to 26%. Of the 12 PSUs, the government will complete the sale of four stand alone refineries before March this year to BPCL and IOC. Besides, the government has already announced that it will not reduce its stake
below 51% in GAIL (Gas Authority of India Ltd), IOC, and ONGC. The rest, which includes BPCL (Bharat Petroleum Corporation Ltd) and HPCL (Hindustan Petroleum Corporation Ltd), it would be decided on a case to case basis. On IBP, Mr Naik said the bids would be invited by this month and depending upon the response, the government will like to complete the sale before March this year (The Indian Express, 13 January 2001).

In January itself, there were press reports that the DoD had recognized the strategic importance of the oil sector, thus giving up the privatization of IOC, ONGC, and GAIL in the foreseeable future. The DoD is content with the sale of just 10% equity in IOC, and even that is not being carried out presently because the market is depressed (The Financial Express, 29 January 2001). Let us take a quick look at the major developments on this issue through the eyes of the media. The DoD had decided to seek the cabinet nod for obtaining guidelines on investment of the stipulated Rs 20 billion norm for bidding a controlling stake in the IBP Ltd. In the case of exploration business, the investment will require to be carried out in seven years from the date of acquisition of IBP, four years in the case of terminals, and three years in the case of refineries and two years in the case of pipelines.

The investment norm is indexed to wholesale price index. The government is considering a proposal to build in greater flexibility into the qualifying investment criteria. So far, the government had been thinking of seeking a bank guarantee for this sum as surety for investment of the stipulated Rs 20 billion ($0.44 billion). Now, it is contemplating a process where, in the event that investment does not take place in a specified time frame, the companies will be given the option to invest the sum in government securities or such instruments for a specified period (The Hindu Business Line, 19 March 2001).

With no decision been taken on the cross holding of stand alone refineries, the government is likely to miss the target of achieving Rs 25 billion ($0.56 billion) revised disinvestment revenue projected for this fiscal. The cross holding of refineries was expected to yield Rs 17 billion ($0.38 billion) to the disinvestment kitty. The problem arises because no decision has still been taken on buying
out all the shares of the four stand alone refineries at Bongaigaon, Chennai, Numaligarh, and Kochi by BPCL, IBP and IOC, even though the fiscal is set to close. Officials of the ministries of petroleum and finance are yet to finalize the share valuation of these companies, without which the sale cannot be completed (Business Standard, 19 March 2001).

The financial jugglery of the government to meet the disinvestment plans seems to have disappointed the stock markets once again. The government move to sell the stakes in three stand alone refineries to big oil companies at a steep price without an open offer to other shareholders has upset the calculations of investors. Share prices of public sector stand alone refineries (Bongaigaon Refineries, Chennai Petroleum and Kochi Refineries) came under selling pressure even as the BSE Sensex remained steady on Monday. "The government's move to exempt the new parents of these units from making an open offer contributed to the downslide in the prices," said an analyst. This is the second time in the last three years that the so called disinvestment in the oil sector has resulted into erosion of wealth for investors. (The Indian Express, 26 March 2001). There is a serious difference of opinion between the petroleum ministry and the department of disinvestment over the eligibility criteria for companies, which want to bid for the IBP stake.

The difference has arisen over the foreign companies, which want to qualify for bidding under the category of those, who 'intend' to invest Rs 20 billion ($434.78 million) in the petroleum sector in the future. The petroleum ministry is of the view that the policy objective of throwing open marketing rights was to use it as an incentive to attract investment in refineries and oil exploration. It has, therefore, taken the stand that investment in market related activities should not be included in the Rs 20 billion ($434.78 million) eligibility criterion. Such a step would contradict the very rationale of the policy. The department of disinvestment, on the other hand, is reported to be of the view that even investments in market related activities should be included towards the overall investment eligibility criterion. They hope to attract more bidders and thereby get a better price for the IBP stake with this more liberal approach. The
'intended' investment criterion has also thrown up the issue of having a foolproof way of ensuring that Rs 20 billion ($434.78 million) is actually invested in the future. The petroleum ministry is of the view that the potential investor should furnish a bank guarantee to fulfill this objective. But the department of disinvestment appears to be of the opinion that no company will offer such a large bank guarantee. An escrow account or some other such facility is also being considered at the inter-ministerial discussions at this stage (The Hindustan Times, 5 May 2001). The government is likely to retain the veto power to safeguard business and employee interest even after off loading 33.58% of its equity to a strategic partner in IBP Co Ltd.

Post disinvestment, the government, with a 26% stake, would be the second largest shareholder after the strategic partner in IBP. The government has made its intent clear in the confidential information memorandum posted to the 13 companies and consortia in race for buying the government's 33.59% stake. The veto power may be used against change of business, employee dismissal, asset stripping, and premature sale. The strategic partner, who would be given managerial control of IBP, would need the government nod on these issues. Besides, the government approval would also be needed for raising debt, public offering, and off loading stake (The Hindu Business Line, 21 June 2001).

The Union Government is set to revert to its original plan for the sale of its 25% equity in IPCL (Indian Petrochemicals Corporation Ltd) to a strategic buyer. The MoD (Ministry of Disinvestment) is looking at continuing with the sale of 25% of the Government's equity in IPCL as a whole with the two bidders left in the fray RIL (Reliance Industries Ltd) and IOC Soros Chatterjee combine. The move to go back to the original proposal for disinvestment in IPCL comes in the wake of an unsuccessful attempt by a disputes committee headed by the Cabinet Secretary to resolve the differences between IPCL and IOC over the valuation of the former's Vadodara plant which was to be transfer it to IOC. The CCD (Cabinet Committee on Disinvestment) had decided last year to alter the IPCL divestment plan by hiving off its Vadodara Plant into a separate entity and transferred to IOC after proper valuation of assets. The CCD had also decided
to retain the 25% strategic sale plan for the remaining two units of IPCL at Nagothane and Gandhar. However, even after a year, both IPCL and IOC have not been able to sort out the differences in valuation for transferring the Vadodara plant to IOC. While IPCL interpreted the transfer as an asset sale and pegged a higher price for its Vadodara plant, IOC clearly stated its willingness to take over the plant only if it was offered at a reasonable price minus all liabilities (The Hindu Business Line, 18 September 2001).

The TERI opinion

The first issue that has to be resolved before disinvestment of oil sector PSUs could proceed is that of the strategic nature of the petroleum sector. After all, this was the ground on which assets of foreign oil companies were nationalized in the 1970s. Now that the assets were being handed back to the private sector, the government needed to be convinced that the concerns of the 1970s were no longer valid. The issue was resolved quickly enough with the decision that the government would continue to hold at least 50% of the shares of IOC, ONGC and GAIL. This would ensure that the government has enough control over this vital sector to intervene, if need be, in times of war or other emergencies. The other important issue is that of decontrol of petroleum product prices. With the decontrol of the price of ATF earlier this year, the price control now applies to gasoline, diesel, domestic LPG and kerosene. These controls are due to be lifted w.e.f. 1st April 2002. In spite of statements issued by the Petroleum and Natural Gas Minister and the Finance Minister, there is some doubt whether the government would go through with decontrol by the announced date. Any rise in the crude oil price following a war in the Middle East may push the date back indefinitely. So long as such an uncertainty continues, it would be difficult for the government to get the best price for its shares. The exercise that is on right now is the disinvestment of IBP shares. These shares are different from shares sold earlier in that the buyer gets a chain of 1600 retail outlets and thereby a strong foothold in petroleum marketing. According to the relevant notification, marketing rights can be available only to those who invest at least Rs 2000 crores in the petroleum
industry. The foregoing note shows that even the interpretation of this condition presents a problem. The benefits from private entry into the petroleum sector go beyond raising resources for the government and we would really like to see such problems solved at the earliest so that some tangible results can be achieved.

**HPCL/BPCL disinvestment: A supreme blow**

THE Supreme Court decision in the HPCL/BPCL disinvestment case will have far reaching consequences on the power of the Central and State Government to sell its shares in government companies. Burma Shell, Esso, and Caltex were nationalised between 1974 and 1977. Three Parliamentary enactments provided for acquisition of the entire undertakings of these three oil companies. As per the preamble to this Act, the ownership and control of all petroleum products, their distribution and marketing were to be vested with the state and thereby so distributed as best to subserve the common good. The Acts were passed in the heyday of socialism. The oil companies were acquired soon after the banking and coal companies were nationalized.

Under the three enactments, all assets and liabilities of the three foreign oil companies vested with the Central Government and, thereafter, with three government companies. Until 1992-93, the Centre virtually held the entire shareholding in HPCL/BPCL. Between 1992-93 and 1993-94, shares in HPCL and BPCL were sold to the public, and quoted in the stock market. The initial sale of shares was not challenged. The decision of the Central Government to disinvest its shareholding in these three companies was challenged mainly on one ground: That these companies were taken over by an Act of Parliament and, therefore, any disinvestment would also require an amendment or modification of the Act under which they were constituted. The Central Government could not exercise its executive powers to disinvest its shares in HPCL/BPCL. It would have to repeal or amend the parent law itself. Writ petitions were filed in public interest directly before the Supreme Court under Article 32. A perusal of the judgment sets out four grounds on which the Supreme Court struck down the proposed disinvestment. First, the language
used in the three enactments did not permit the Central Government to disinvest its shares without repealing or amending the respective Acts.

The reasons given in the judgment are simply not correct. Once the oil companies were taken over, all the assets and liabilities vested with three government companies. The Central Government became the owner of all the assets and also had to discharge all the liabilities. Once a government company is formed, it is not necessary that it should remain a so forever. Interestingly, the enactments nationalising banks and coal mines specifically stated that shareholding of the Central Government shall not be less than 51 per cent of any government company that is formed to run a banking or coal business. Thus, such companies will always be government companies and any disinvestment below this percentage will require Parliament's approval.

Such a provision was conspicuously absent while taking over the oil companies though bank and coal nationalisation had preceded the take over of the oil companies. Therefore, Parliament had deliberately not chosen to include such a restriction. Strangely, the Supreme Court held that a specific power should have been conferred under the Act itself to enable disinvestment of shares. This is clearly incorrect; if no restriction is placed on the percentage and when no requirement of holding 51 per cent shareholding is imposed, it follows that there cannot be any prohibition against disinvestment of shares in HPCL/BPCL. Second, the Supreme Court referred to Article 113 of the Constitution and Rule 71 of the General Finance Rules. Under these provisions, the setting up of new public sector companies requires the approval of Parliament for expenditure from the Consolidated Fund of India. The Supreme Court held that if a government company was formed with parliamentary approval, it could not be "dismantled without some kind of parliamentary mandate". If this logic is accepted, any assets acquired with parliamentary approval can never be sold without parliamentary approval.

Third, the Supreme Court stated that the three enactments taking over the oil companies provided for the assets and liabilities to vest in government companies. Therefore, it would mean that the ownership or control must always
be with the government company. This reasoning is also incorrect. When Parliament wanted certain sectors to be controlled by government companies, it had made an express provision, as in the case of banks and coal mines. If the Centre has taken a policy decision to disinvest its shares, there is no statutory provision that requires parliamentary approval before it can do so. It is elementary principle of jurisprudence that the owner of an asset has the right to sell, lease or mortgage it. If the Central Government is the owner of an asset, it can always sell its shares exercising its rights as an owner. If the Supreme Court's logic is accepted, then for any sale or even lease of assets, we will have to go back to Parliament for approval or a specific provision must be made in the Parliamentary Act itself.

Maruti Udyog Ltd. was also taken over by an Act of Parliament but the disinvestment was completed without amending the parent Act. The Supreme Court observed that the Maruti disinvestment had not been challenged. Similarly, the disinvestment in BALCO was not challenged presumably because there was no Act of Parliament. Therefore, these "two cases stood on a different footing". Maruti certainly stands on the same footing. If the HPCL/BPCL disinvestment is not valid, the Maruti disinvestment must also fail. The Supreme Court has not stated that its decision will have prospective effect. This is a dangerous feature that requires clarification. The decision of the Supreme Court requires to be reconsidered by means of a review petition.

The Supreme Court judgment will have disastrous consequences for the disinvestment process both at the Centre and the States. It will make several politicians happy as state control translates into political patronage and enormous benefits to politicians, their relatives and associates and their favourite bureaucrats. With the state of political uncertainty and divergent viewpoints on disinvestment even in the ruling NDA Government, the disinvestment process will be a in a coma for a long time to come.
ONGC keen on HPCL, BPCL stake

OIL and Natural Gas Corporation (ONGC) is interested in bidding for Bharat Petroleum Corporation Ltd (BPCL) and Hindustan Petroleum Corporation Ltd (HPCL), according to ONGC Chairman and Managing Director, Mr Subir Raha. However, while the Government has already banned Indian Oil Corporation (IOC) from bidding for BPCL and HPCL, the Disinvestment Ministry is keen on banning public sector undertakings from bidding for the two companies. In this context, Mr Raha said that he had sought equal opportunity vis-a-vis the private sector from the Government to participate in the privatisation process of the two oil majors. On the exploration front, ONGC plans to invest $2 billion annually for the next 7-10 years to double the in-place reserves to 12 billion tonnes of oil and oil equivalent gas. Speaking at a conference on oil and gas here, Mr Subir Raha said: "We plan to double in-place reserves of 5.77 billion tonnes of oil and oil equivalent gas through extensive exploration efforts, particularly in deep-waters."

Pitching for early decontrol of natural gas prices by the Government, Mr Raha said that the investment targets could be met only "when the company gets market price for its production". "Genuine deregulation of gas has not taken place as natural gas prices are still tightly controlled by the Government," he added. Oil accounts for about 34 percent of India's total energy consumption, and has been growing gradually as a share of the country's fuel mix in recent years. The majority of India's roughly 5.4 billion barrels in oil reserves are located in the Mumbai High, Upper Assam, Cambay, Krishna-Godavari, and Cauvery basins. The offshore Mumbai High field is by far India's largest producing field. Normal output at Mumbai High is around 275,000 barrels per day (bbl/d), but an offshore gathering platform at the field was damaged in a fire in July 2005. India's state-owned Oil and Natural Gas Corporation (ONGC) expects to have repairs completed by March 2006.
In the meantime some output has been rerouted through other gathering platforms. India's average oil production level (total liquids) for 2005 was 837,000 bbl/d, of which 632,000 bbl/d was crude oil. India had net oil imports of nearly 1.7 million bbl/d in 2005.

Future oil consumption in India is expected to show strong growth, to 3.1 million bbl/d by 2010, from 2.5 million bbl/d in 2005. India is attempting to limit its dependence on oil imports somewhat by expanding domestic exploration and production. To this end, the Indian government is pursuing the New Exploration Licensing Policy (NELP), first announced in 1997, which permits foreign involvement in exploration, an activity long restricted to Indian state-owned firms. While the initial response to the 1999 tender was disappointing, with no bids received from the major multinational oil companies (causing an extension of the deadline for submission of bids), India proceeded with the award of 25 oil
exploration blocks in early January 2000. The largest winner in the bidding round was India's domestic Reliance Industries, in partnership with independent Niko Resources of Canada, which received 12 blocks. British independent Cairn Energy, Russia's Gazprom, the U.S. firm Mosbacher Energy, and Geopetrol of France were all awarded single blocks in partnership with Indian firms. ONGC was awarded eight blocks, three of which it will hold in partnership with other public-sector Indian firms.

A second round of bidding, with a total of 25 blocks offered, concluded in March 2001. Sixteen of the blocks have been awarded to ONGC, and four blocks to Hardy Oil of the United Kingdom, in partnership with India's Reliance Petroleum. The others were either awarded to smaller independent firms or failed to receive bids. As with the first round, no bids were received from major international oil companies. Bids for the third round were received in August 2002, with a total of 27 blocks offered. Awards under this third round were made in February 2003, with domestic Indian firms receiving most of the blocks. Reliance Industries received nine offshore blocks, one adjacent to the Krishna-Godavari Basin. ONGC was awarded 13 blocks, five offshore and eight
onshore. The Gujarat State Petroleum Corporation received one. Blocks offered during the fourth round in 2003 received relatively little foreign interest. Awards for 15 blocks were made in February 2004, with 14 going to ONGC and one going to Reliance Industries. A fifth round of bidding closed in July 2005, with firms receiving the 20 blocks offered in September 2005 including Cairn Energy, Niko Resources, and Italy’s ENI. Low drilling recovery rates are a major part of the oil supply problem for India. Historically, recovery rates have averaged only around 30 percent in currently producing Indian oilfields, well below the world average. It is hoped that allowing foreign investment will bring in technology that is not available to Indian state firms, thereby increasing overall recovery rates. ONGC currently is undertaking a project to increase recovery rates in the Mumbai High offshore field and several others as well, aiming to boost the overall recovery rate for its production assets from 28 percent to 40 percent.

One area which has shown promise is western Rajasthan. Cairn Energy (UK) has been drilling in the area since 2001, and has reported several successful wells in 2004. The Mangala field has been estimated to contain as much as 320 million barrels of recoverable reserves, and the “N-A” field has estimated recoverable reserves of 80 million barrels. Cairn is continuing exploration in the area, and is planning to bring the field into production by early 2008, with an expected volume of 100,000 bbl/d. In February 2002, BG purchased a 30 percent stake in the Panna, Mukta, and Tapti offshore oil and gas fields, which had previously been held by Enron. A dispute between BG and ONGC (which owns a 40 percent interest in the fields) over which firm would operate them was resolved in February 2003 with a “joint operatorship agreement.” Reliance Industries holds the other 30 percent stake.

Downstream/Refining

For most of the 1990s, India imported a large quantity of refined products, as it lacked the refining capacity to keep up with growing demand. In 1999, refinery
construction allowed India to close the gap. At the end of 2004, India had a total of 2.3 million bbl/d in refining capacity, an increase of 1.1 million bbl/d since 1998. The largest single addition was Reliance Petroleum's huge Jamnagar refinery, which began operation in 1999. Jamnagar has since reached its full capacity of 660,000 bbl/d. Jamnagar sells its products through three of the state-owned firms, and also has a retail network of its own. Another major downstream infrastructure development is the construction of pipelines being undertaken by Petronet India, a company created by an agreement in 1998 between India's state-owned refineries. This construction is expected to add 500,000 bbl/d to India's current 325,000 bbl/d capacity for pipeline transportation of refined products. Pipelines between refineries and major urban centers are replacing rail cars as the main mode of transportation in India.

Several multinationals have entered the Indian lubricants market, which was deregulated six years ago. Firms such as Shell, Exxon Mobil, and Caltex currently hold over one-third of the market. While these operations are relatively small, they are seen as allowing the majors to study the Indian market, establish brand recognition, and prepare for the eventual deregulation of the Indian retail petroleum products sector. Still, a requirement that foreign firms invest at least $400 million before entering the downstream market has served to limit their entry into petroleum products retailing. Shell met this requirement in early 2004, and has opened its own retail outlets, though it has slowed its expansion due to the continuance of price controls on petroleum products.

Industry Restructuring and Price Deregulation

The Indian government officially ended the Administered Pricing Mechanism (APM) for petroleum product prices in April 2002. Prior to this deregulation, the Indian government had tried to offset the effects of price changes in crude oil by maintaining an Oil Pool Account, which was to build financial reserves when
crude oil prices fell and release them back as increased subsidies when crude oil prices rose.

In practice, though, the April 2002 reforms have not completely removed government influence on petroleum product prices. Subsidies have been maintained on some products, such as kerosene, which is commonly used as a cooking fuel by low-income households in India. State-owned downstream companies also still must submit proposed price changes to the Ministry of Petroleum and Natural Gas for approval. This has, in practice, limited movements in retail prices in response to fluctuations in world oil prices. The previously planned sell off of government stakes in Hindustan Petroleum (HPCL) and Bharat Petroleum (BPCL) appear unlikely to move forward in the near future. The policy of the new Congress-led government is to avoid most further privatizations of public companies which are making a profit. India is planning to set up a strategic petroleum reserve equal to 15 days of the country's oil consumption. The state-owned refiner Indian Oil Corporation (IOC) is likely to take the lead in the development of the reserve, which would be paid for by the Indian central government by means of a tax on petroleum product sales.