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Oil Bonds and India's Fuel Pricing Regime

Why in news?

The Centre has argued that it cannot reduce taxes on petrol and diesel as it has to bear the burden of payments with respect to oil bonds issued by the previous UPA government.

What are oil bonds?

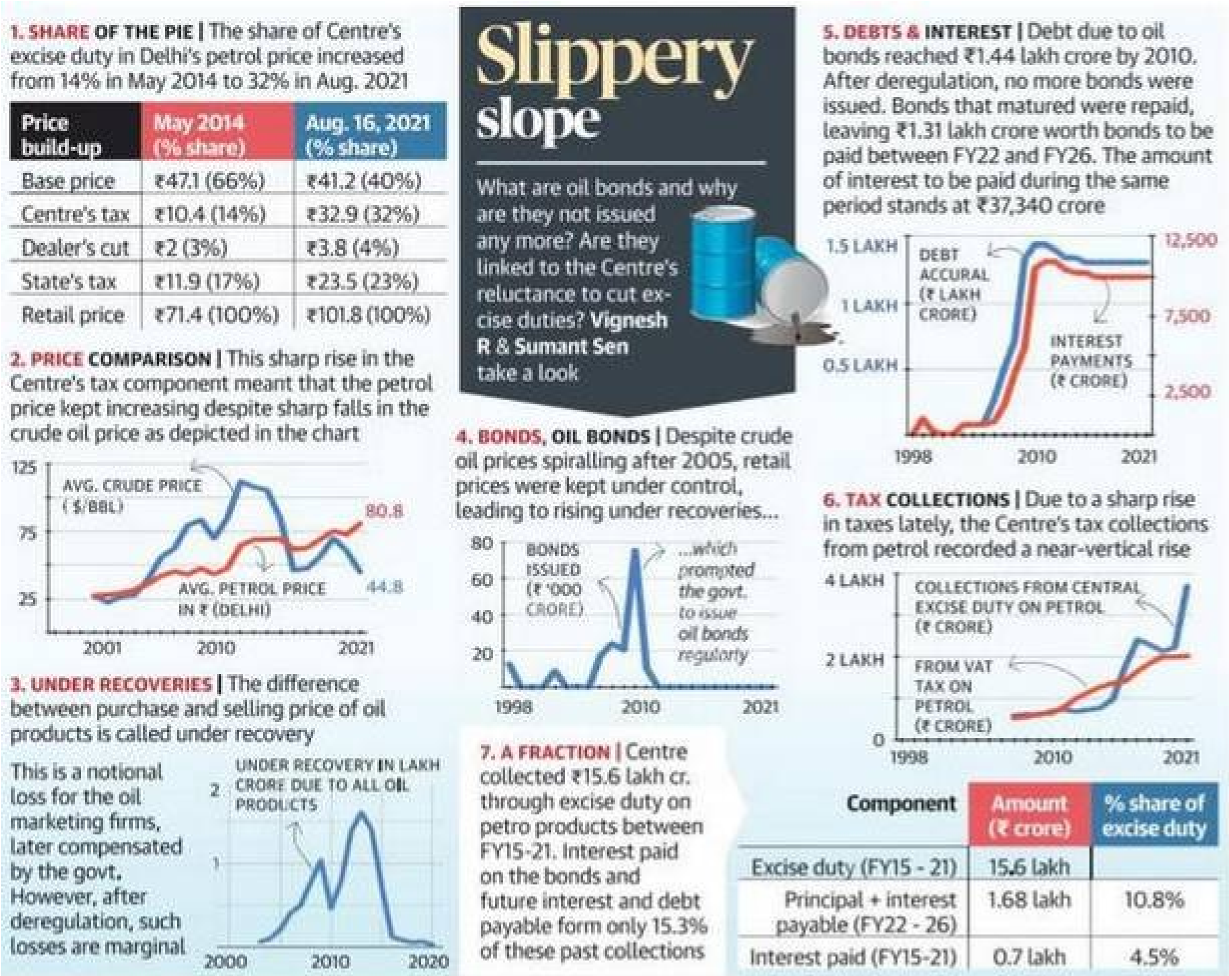
- Oil bonds are special securities issued by the government to oil marketing companies instead of cash subsidy.
- These bonds are typically of a long-term tenure like 15-20 years and oil companies are paid interest.
- Governments resort to such instruments when they are in danger of breaching the fiscal deficit target.
- These types of bonds are considered to be 'below the line' expenditure in the Union budget and do not have a bearing on that year's fiscal deficit, but they do increase the government's overall debt.
- The interest payments and repayment of these bonds become a part of the fiscal deficit calculations in future years.

How has India's fuel pricing regime evolved in recent years?

- Before the complete deregulation of fuel prices, oil marketing companies faced a huge financial burden as the selling price of fuels in India was lower than the international market price.
- The story of dismantling oil prices started from 1997 when the government thought of moving from an administered price mechanism of cost-plus pricing to market-determined consumer prices for fuels.
- The Nirmal Singh Committee made recommendations in 1996 and it was decided that the oil pricing mechanism would be dismantled gradually from 1997 till 2002.
- Full dismantling as oil prices were announced in 2002.
- From 2004, oil prices started moving up, and the government restored the cost-plus pricing system to protect consumers.
- The government subsidised the prices for transport fuels, LPG and kerosene through a mechanism to provide for oil marketing companies' under-recoveries.
- Between 2005 and 2010, the UPA government issued oil bonds to the companies amounting to Rs 1.4 lakh crore to compensate for the losses.

What is the current issue with oil bonds?

- Prices of petrol and diesel are climbing steeply and the Centre has been under pressure to cut the high taxes on fuel.
- The price of petrol has been increased 39 times and decreased once in 2021-22, while that of diesel has been increased 36 times and decreased twice.
- The government has so far been reluctant to cut taxes as excise duties on petrol and diesel are a major source of revenue.
- It pointed out that the bonds issued by the UPA government have weakened the financial position of the oil marketing companies and added to the government's fiscal burden now.
- The government has to repay a principal amount of Rs 10,000 crore this year in addition to Rs 10,000 crore paid annually as interest over the last decade.
- Budget documents show that such bonds will be up for redemption over the next few years till 2026.



What are the reasons for high price of fuels currently?

- **Taxes-** The higher level of excise on transport fuels has led to higher VAT levies in States, which have in turn increased the prices.
- Taxes account for 58% of the retail selling price of petrol and 52% of the retail selling price of diesel.
- **Depreciation of rupee**- The Rupee has depreciated in the recent past adding to the increased cost.
- **Increased share of energy imports**- The share of energy imports has gone from 70% to

86%-87%.

- **Supply issues**- The OPEC countries are not releasing production quotas since COVID-19.
- **International issues**- Ukraine-Russia crisis is also a key factor for the high prices.

What other bonds of similar nature have been issued earlier?

- **Fertiliser bonds**- The fertiliser bonds were issued from 2007 to compensate fertiliser companies for their losses due to the difference in the cost price and selling price.
- **Bank recapitalisation bonds**- The NDA government has issued bank recapitalisation bonds to specific public sector banks (PSBs) to meet the large capital requirements of these PSBs without allocating money from the budget.
- **NSSF**- The ruling government used the National Small Savings Fund (NSSF) to finance its food subsidy bill outside of the budget.
- From 2016-17 to March 2021, the Food Corporation of India borrowed from NSSF to finance the food subsidy.

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