

# THE PRS BLOG » EXPLAINED: THE RECENT RISE IN PETROLEUM PRICES

Relevant for: World & Indian Geography | Topic: Distribution of key natural resources - Mineral & Oil Resources in world & India

In the past few months, retail prices of petrol and diesel have consistently increased and have reached all-time high levels. On September 24, 2018, the retail price of petrol in Delhi was [Rs 82.72/litre](#), and that of diesel was [Rs 74.02/litre](#). In Mumbai, these prices were even higher at [Rs 90.08/litre](#) and [Rs 78.58/litre](#), respectively.

The difference in retail prices in the two cities is because of the different tax rates levied by the respective state governments on the same products. This blog post explains the major tax components in the price structure of petrol and diesel and how tax rates vary across states. It also analyses the shift in the taxation of these products, its effect on retail prices, and the consequent revenue generated by the central and state governments.

## What are the components of the price structure of petrol and diesel?

Retail prices of petrol and diesel in India are revised by oil companies on a daily basis, according to changes in the price of global crude oil. However, the price paid by oil companies makes up 51% of the retail price in case of petrol, and 61% in the case of diesel (Table 1). The break-up of retail prices of petrol and diesel in Delhi, as on September 24, 2018, shows that over 45% of the retail price of petrol comprises central and states taxes. In the case of diesel, this is close to 36%.

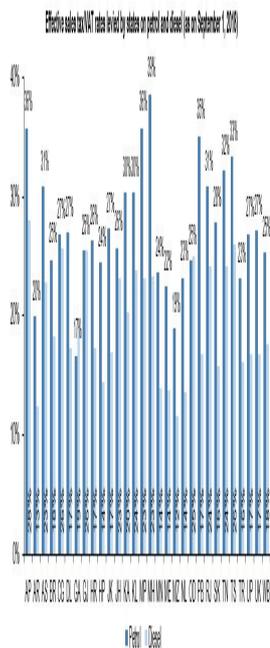
At present, the central government has the power to tax the production of petroleum products, while states have the power to tax their sale. The central government levies an excise duty of Rs 19.5/litre on petrol and Rs 15.3/litre on diesel. These make up 24% and 21% of the retail prices of petrol and diesel, respectively.

Table 1: Break-up of petrol and diesel retail prices in Delhi (as on September 24, 2018)

Component	Petrol		Diesel	
	Rs/litre	% of retail price	Rs/litre	% of retail price
Price paid by oil companies	42.0	51%	45.3	61%
Excise Duty (levied by centre)	19.5	24%	15.3	21%
Commission of oil companies	3.7	4%	2.5	3%
Sales Tax/VAT (levied by state)	17.0	21%	11.9	16%
<b>Retail Price</b>	<b>82.7</b>	<b>100%</b>	<b>74.0</b>	<b>100%</b>

Source: Indian Oil Corporation Limited, PRS.

While excise duty rates are uniform across the country, states levy sales tax/value added tax (VAT), the rates of which differ across states. The figure below shows the different tax rates levied by states on petrol and diesel, which results in their varying retail prices across the country. For instance, the tax rates levied by states on petrol ranges from 17% in Goa to 39% in Maharashtra.



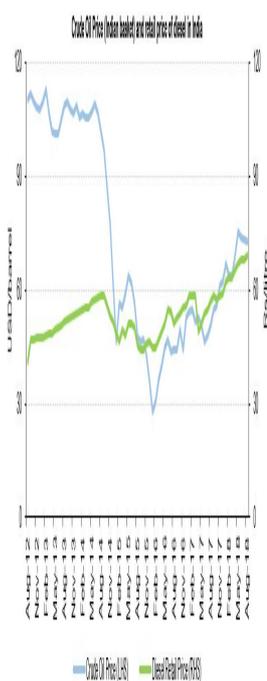
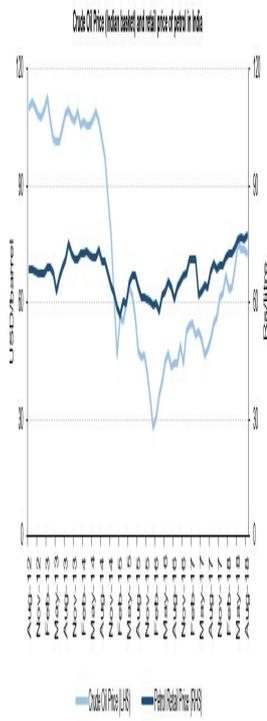
Note: The rates shown for Karnataka are average of the rates levied in Mumbai, Thane region and in the rest of the state.  
 Source: Petroleum Planning and Analysis Cell, Ministry of Petroleum and Natural Gas, 2016.

Note that unlike excise duty, sales tax is an ad valorem tax, i.e., it does not have a fixed value, and is charged as a percentage of the price of the product. This implies that while the excise duty component of the price structure is fixed, the sales tax component is charged as a proportion of the price paid by oil companies, which in turn depends on the global crude oil price. With the recent increase in the global prices, and subsequently the retail prices, [some states such as Rajasthan, Andhra Pradesh, West Bengal, and Karnataka have announced tax rate cuts.](#)

### How have retail prices in India changed vis-à-vis the global crude oil price?

India's dependence on imports for consumption of petroleum products has increased over the years. [For instance, in 1998-99, net imports were 69% of the total consumption, which increased to 93% in 2017-18.](#) Because of a large share of imports in the domestic consumption, any change in the global price of crude oil has a significant impact on the domestic prices of petroleum products. The following figures show the trend in price of global crude oil and retail price of petrol and diesel in India, over the last six years.





Note: Global Crude Oil Price is for the Indian basket. Petrol and diesel retail prices are for Delhi. Figures reflect average monthly price.  
Source: Petroleum Planning and Analysis Cell, Ministry of Petroleum and Natural Gas, PSU.

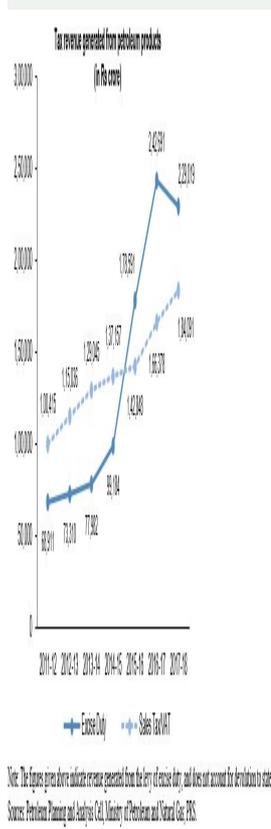
The global price of crude oil (Indian basket) decreased from USD 112/barrel in September 2012 to USD 28/barrel in January 2016. Though the global price dropped by 75% during this period, retail prices of petrol and diesel in India decreased only by 13% and 5%, respectively. This disparity in decrease of global and Indian retail prices was because of increase in taxes levied on petrol and diesel, which nullified the benefit of the sharp decline in the global price. Between [October 2014](#) and [June 2016](#), the excise duty on petrol increased from Rs 11.02/litre to Rs 21.48/litre. In the same period, the excise duty on diesel increased from Rs 5.11/litre to Rs 17.33/litre.

Over the years, the central government has used taxes to prevent sharp fluctuations in the retail price of diesel and petrol. For instance, in the past, [when global crude oil price has increased, duties have been cut](#). Since January 2016, the global crude oil price has increased by 158%

from USD 28/barrel to USD 73/barrel in August 2018. However, during this period, [excise duty has been reduced only once by Rs 2/litre in October 2017](#). While [the central government has not signalled any excise duty cut so far](#), it remains to be seen if any rate cut will happen in case the global crude oil price rises further. With US economic sanctions on Iran coming into effect on November 4, 2018, [India may face a shortfall in supply](#) since [Iran is India's third largest oil supplier](#). Moreover, [Organization of Petroleum Exporting Countries \(OPEC\) and Russia have not indicated any increase in supply from their side yet to offset the possible effect of sanctions](#). As a result, in a scenario with no tax rate cut, this could increase the retail prices of petrol and diesel even further.

## How has the revenue generated from taxing petroleum products changed over the years?

As a result of successive increases in excise duty between November 2014 and January 2016, the year-on-year growth rate of excise duty collections increased from 27% in 2014-15 to 80% in 2015-16. In comparison, the growth rate of sales tax collections was 6% in 2014-15 and 4% in 2015-16. The figure below shows the tax collections from the levy of excise duty and sales tax on petroleum products. From 2011-12 to 2017-18, excise duty and sales tax collections grew annually at a rate of 22% and 11%, respectively.



## How is this revenue shared between centre and states?

Though central taxes are levied by the centre, it gets only 58% of the revenue from the levy of these taxes. The rest 42% is devolved to the states as per the recommendations of the 14th Finance Commission. However, excise duty levied on petrol and diesel consists of two broad components – (i) excise duty component, and (ii) road and infrastructure cess. Of this, only the revenue generated from the excise duty component is devolved to states. Revenue generated by the centre from any cess is not devolved to states.

The cess component was [increased by Rs 2/litre to Rs 8/litre in the Union Budget 2018-19](#). However, this was done by reducing the excise duty component by the same amount, so as to

keep the overall rate the same. Essentially this provision shifted the revenue of Rs 2/litre of petrol and diesel from states' divisible pool of taxes to the cess revenue, which is entirely with the centre. This cess revenue is earmarked for financing infrastructure projects.

At present, of the Rs 19.5/litre excise duty levied on petrol, Rs 11.5/litre is the duty component, and Rs 8/litre is the cess component. Therefore, accounting for 42% share of states in the duty component, centre effectively gets a revenue of Rs 14.7/litre, while states get Rs 4.8/litre. Similarly, excise duty of Rs 15.3/litre levied on diesel consists of a cess component of Rs 8/litre. Thus, excise duty on diesel effectively generates revenue of Rs 12.2/litre for the centre and Rs 3.1/litre for states.

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