Mukesh Kacker: Will the petroleum regulator stand up?

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Much has already been written about how regulation of anti-competitive behaviour leads to increased allocative efficiencies and consumer welfare. Less, however, seems to have been written on whether the structures of regulation put in place secure these desirable ends.

This is particularly true of India where independent regulation is of relatively recent origin. It will be worthwhile to take a close look at the state of regulation in the petroleum and natural gas sector, which has been consistently in the news of late.

The petroleum sector consists of four sub-sectors, namely, exploration and production, oil refining and marketing, natural gas transportation and marketing, and crude oil and petroleum products pipelines. Of these four, the first, referred to as upstream, is supposed to be regulated by the Directorate General of Hydrocarbons (DGH), while the remaining three downstream sub-sectors fall under the domain of the Petroleum and Natural Gas Regulatory Board of India (PNGRB).

The DGH was created by a government resolution in 1993 and was posited as the regulator of the upstream sector. Nothing could be farther from the truth. It is neither independent nor a regulator. When the instrument of creation, a Ministry of Petroleum and Natural Gas order, derives its genesis from a mere resolution, rather than a statute, then independence would remain an illusory concept. The DGH operates under direct and complete administrative control of the ministry. It functions with the assistance of an advisory council and members of the council and staff of the DGH are appointed on a deputation/tenure basis by the ministry in consultation with the DGH chief. In terms of its mandate, the DGH is predominantly an advisory, rather than a regulatory, body. As per the ministry order, the DGH has been mandated to regulate only one area — preservation, upkeep and storage of data and samples pertaining to petroleum exploration, drilling, production of reservoirs et cetera and to cause the preparation of data packages for acreages on offer to companies. In all other areas relating to various aspects of exploration and production, it is only supposed to advise the ministry.

In the downstream sector, we have a genuine regulator, owing its existence to a statute and not to a mere resolution. The Petroleum and Natural Gas Regulatory Board Act was passed in 2006 and the PNGRB was notified on October 1, 2006. The PNGRB has been vested with very tangible regulatory powers and the statutory nature of its genesis gives it its independence. But despite its powers and independence, it is the ministry which seems to call the shots in the regulatory space. Before March 28, 2002, marketing and pricing of petroleum products, including transportation fuels, namely, motor spirit (MS) and high-speed diesel (HSD), was controlled by the government under a mechanism known as “Administered Price Mechanism (APM)”. The APM was dismantled by a notification on March 28, 2002. As a result, the theoretical position since October 1, 2006 is that all entities are free to price their products and the PNGRB is to regulate anti-competitive behaviour like predatory pricing. However, strangely, the government still fixes the prices of MS and HSD and the PNGRB appears to be either powerless or disinterested in

doing anything about it. How can the government fix these prices now? What is the role of the PNGRB?

These issues have been examined brilliantly in a landmark judgment, dated October 5, 2009, by the Appellate Tribunal for Electricity, in appeal number 50 of 2009. The judgment, either directly or indirectly, establishes the following positions:

* Sections 11(a), 12 and 25 of the PNGRB Act, 2006, together give a wide amplitude to its duties and powers to foster fair trade and fair competition amongst the entities.

* The dismantling of the APM by the notification dated March 28, 2002 was a policy decision which has not been reversed by another policy decision. The government, therefore, cannot fix prices under the garb of policy.

* Section 2(x) of the Act specifically provides that it is only the entities which can fix the price and not the government.

* The above power given to the entities to fix the price cannot be usurped by the government.

* If the prices are to be fixed by the government as a sovereign, then it has to be declared as a public policy after observing formalities as provided under the Constitution.

After this judgment by the tribunal, the case is now before the PNGRB. It will be interesting to see whether the PNGRB asserts its independence and buries the ghost of APM once and for all.

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