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## Fuelling the Future: Landscape, Challenges, and Tax Optimisation in the Oil and Gas Industry

India’s oil and gas sector, a prospective \$8.6 trillion GDP market, fuels the economy but grapples with tax inefficiencies. Exclusion from GST denies utilisation of ITC, leading to a cascading tax burden and ultimately an increase in the cost of fuel. Additionally, states’ reliance on petroleum tax revenue makes them reluctant to transition to GST. Considering the uncertainty of GST integration and the unavailability of ITC, the industry

must leverage the exemptions and concessions available under GST to structure transactions efficiently. While concerns over revenue loss exist, a balanced approach of integrating tax reforms with fiscal incentives can transform the sector. Proactive reforms today will ensure a resilient energy future tomorrow.

### Introduction

Amidst a rapidly evolving global landscape, one sector has emerged as a linchpin of India’s economic framework. An industry that not only fuels the ambitions of a growing nation but also positions itself as a critical player on the global stage. The industry, which is expected to reach \$8.6 trillion GDP by 2040, exported 64.7 MMT of products while producing 264 MMT domestically. Drawing \$8.22 billion in cumulative FDI inflows since 2000, this sector underpins the nation’s foreign reserves and industrial backbone as one of the eight core industries. The Oil and Gas Exploration Industry drives India’s energy future in every aspect of growth, right from revenue to returns, investments to international trade and from forex to fiscal contributions.

The industry operates across three interconnected sectors.

- The upstream sector
- The midstream sector
- The downstream sector

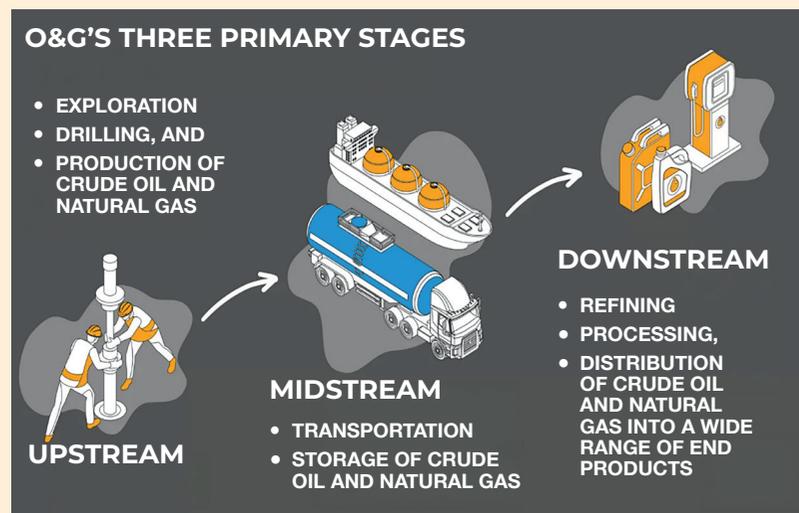
The industry, being heavily regulated, also requires massive capex in exploration and infrastructure

development. However, the pressing concern of the industry is upon the taxation policies implemented on them. With varied taxes and duties imposed without adequate benefits, especially under Indirect taxes, the members consistently urge the ministries to consider their hardships.

### Levy of Indirect Taxes in the Industry

Until the implementation of the Goods and Services Tax Act, 2017 (hereinafter referred to as “The CGST

Act, 2017 or “The Act”), multiple indirect taxes were levied by both the Central and State governments, leading to inefficiencies and cascading effects. The CGST Act, 2017, unified varied taxes as one single tax. However, vide Article 279A (5) of the Constitution and Section 9(2) of the Act, the Central Board of Indirect Taxes and Customs (hereinafter referred to as “CBIC”) deferred petroleum crude, high speed diesel, motor spirit, natural gas and aviation turbine fuel from GST.



Further, Article 246 of the Constitution grants power to the Parliament and the Legislatures of States to make laws with respect to matters under the Seventh Schedule. While entry no. 84 of the Union List empowers the Central Government to levy excise duty, entry no. 54 of the State List allows the State Government to impose VAT on the aforementioned goods. This has resulted in a situation wherein petroleum products are taxed separately through different taxes, and that too at different rates.

This exclusion of petroleum products from the ambit of GST has deferred the Government's vision of implementing the "One Nation, One Tax" policy. The introduction of GST aimed to unify taxation, reduce the cascading effect, and establish an efficient tax collection system, which currently seems to be defeated.

Since inputs required for production are taxed under GST while outputs are excluded, the break in the Input Tax Credit (hereinafter referred to as "ITC") chain adds a significant cost burden. As of 2025, India, the third-largest oil consumer, faces higher

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fuel prices due to this cascading tax effect. One of the key reasons for inflated fuel costs is the inability to offset input taxes, increasing the overall financial strain on the industry and consumers. To illustrate this, a detailed cost breakup of petrol and diesel as applicable in the State of Maharashtra is provided in Table 1.

Given that the petroleum product prices are generally determined by global benchmarks such as Brent Crude and WTI, the cost of

the products cannot be increased arbitrarily, ultimately leading to the cost of input taxes being absorbed by the industry.

The Federation of Indian Petroleum Industry (FIPI) has been actively advocating for the industry's concerns regarding GST exclusion. FIPI, a society representing hydrocarbon sector entities, serves as an interface with the government. According to a report for FY. 2021-22, "exclusion from the GST regime and dealing with multiple taxes has resulted in a cascading tax effect, reversal of ITC, leaving the industry stranded with taxes as high as 60%." Given the uncertainty surrounding GST inclusion, the industry must thoroughly assess contracts, meticulously examine invoices, and accurately determine tax rates to minimize procurement costs effectively.

### Tax Optimisation Strategies

Industry relies heavily on specialised services and complex equipment, making cost and financial liquidity the foremost deciding factor. Industry's versatile landscape requires services like Front End Engineering Design

**Table 1**

Particulars	Cost per litre	
	Petrol Price	Diesel Price
Crude Oi1 (from Brent Crude + Russian Import + Other Crude Import)	Rs. 40	Rs. 40
OMC Processing Cost (Freight + Refinery Processing + OMC Margin + Logistics Operational Costs)	Rs. 7.35	Rs. 8.15
Buffer for Future Inflationary Aspect etc	Rs. 10	Rs. 8
<b>Fuel Price after processing (A)</b>	<b>Rs. 57.35</b>	<b>Rs. 56.15</b>
<b>Central Government Taxes and Dealer Commission</b>		
Excise Duty (all inclusive) + Road Cess as Charged by Central Government	Rs. 19.9	Rs. 15.8
Commission to Petrol Pump Dealers	Rs. 3.8	Rs. 2.6
<b>Fuel Cost Before VAT</b>	<b>Rs. 81.05</b>	<b>Rs. 74.55</b>
<b>State Taxes (Maharashtra)</b>		
Vat@ 25% on petrol/ Vat@ 21% on diesel	Rs. 20.26	Rs. 15.65
Additional tax	Rs. 5.12	-
<b>Final Retail Price in Mumbai (B)</b>	<b>Rs. 106.43</b>	<b>Rs. 90.60</b>
<b>Proportion of Total Tax to Final Cost</b>	<b>42.5%</b>	<b>34.71%</b>



Services, also known as FEED services in the upstream sector, pipeline construction and maintenance in the midstream sector and product distribution in the downstream sector. Given its capital-intensive nature and the unavailability of ITC, optimizing taxes becomes a key consideration.

#### i. Relaxation of IGST for Goods Imported under Lease

Certain goods integral to exploration operations are required to be imported, often incurring significant costs in the form of customs duties. CBIC vide NN 50/2017-Customs introduced entry 557A and 557B, levying a Nil rate of IGST for specified goods. This exemption applies to rigs imported for oil or gas exploration and production under lease agreements.

However, the exemption is conditional. The importer must re-export the goods within three months from the expiry of the lease. Failure to comply would result in the payment of applicable duties as if the goods were imported under normal circumstances. Therefore, strict adherence to these conditions is essential to retain the benefits.

#### ii. Maintenance, Repair or Overhaul services (MRO) for ships and vessels

The industry often ensures that imported vessels are ready for use by maintaining and repairing them before shipping, reducing reliance on local repair services

and affecting domestic sales and tax revenues. Usually, such services are exigible at a rate of 18%, thereby increasing the industry's cost burden. To create a level playing field, CBIC issued NN.02/2021-CTR, establishing a concessional 5% rate on MRO services for ships, vessels, engines, etc. Vessels such as drillships, anchor handling tug vessels, and FPSO units can benefit from this notification. However, it is important to determine whether the goods qualify as "vessels".

Furthermore, NN. 03/2021-CTR clarified that the POS for these services shall be the location of the recipient. This allows suppliers to benefit from export provisions under the IGST Act where the recipient is a foreign entity. This ultimately benefits both the service providers and recipients of services provided to incoming foreign vessels.

### Destiny Redefined: The Industry Transformation

The industry significantly contributes to the exchequer through royalty and cess over and above the direct and indirect taxes. With continued performance and persistent representation, CBIC provided certain reliefs; however, all such reliefs have now been snatched away from the industry- thanks to the government's decision to expel the 12% tax rate. This decision has not only added to the cost burden for the companies operating in this sector but also increased the intricacies, which are outlined below:

“As GST is a destination-based tax, the inclusion would shift revenue from oil-producing states to consuming states, creating concerns about revenue distribution.”

#### i. Concessional Rate on Specified Goods

With petroleum exploration requiring a range of goods, CBIC offered a concessional tax rate on specified goods that are integral to exploration projects, vide NN. 03/2017-CTR. The said notification set a concessional rate of 5% on goods essential for petroleum operations, which were later amended to 12% vide NN 08/2022-CTR effective from 18.07.2022. Further, vide NN.11/2025-CTR, the tax rate has been amended to 18% w.e.f 22.09.2025.

While the previous rate benefited a wide array of equipment from technical drawings and jack-up rigs, the updated tax rate provides no comfort to the industry. The changes in tax rate shall also impact the IGST payable on imports made under Sr No. 404 of NN.50/2017-Customs, which shall also increase from 12% to 18%.

One of the questions arises as to how one should proceed when the same commodity is subject to varying tax rates. Consider helicopters. As per NN. 09/2025 - CTR, these goods attract a 5% tax rate under Sr No. 463 in Schedule I. However, vide NN. 11/2025 - CTR, the same goods carry a 18% rate. This presents a dilemma: should the industry follow the general notification with a lower rate or the specific exemption notification, which imposes additional conditions and a higher rate? Additionally, it is essential to examine the legal basis for



such notifications. NN. 03/2017 - CTR, issued under Section 11(1) of the CGST Act, grants CBIC the power to exempt goods or services. However, instead of providing relief, the tax rates have been increased and that too under conditional circumstances, which include obtaining an Essentiality Certificate issued by the DGH. Navigating these complexities requires a precise understanding of both legislative intent and practical application, elements that can be easily misinterpreted without specialized expertise.

## ii. Offshore Works Contract Services

Before understanding the change, it is important to distinguish between offshore and onshore services. Offshore activities refer to operations that are carried out in the water bodies, typically in deep water, which include services like exploration, drilling, extraction, etc. Onshore activities, on the other hand, are conducted on land. Depending on the location of oil fields, both onshore and offshore exploration can be conducted.

During exploration, certain equipment cannot be purchased directly from vendors, necessitating specialized engineers for the manufacturing

and fabrication of goods. These services, which involve the supply of goods, may result in the construction of immovable property, potentially qualifying as works contracts under Section 2(119) of the Act. To address this, CBIC issued NN. 39/2017- ITR, providing a concessional tax rate of 12% on the composite supply of offshore works contracts relating to oil and gas exploration in the area beyond 12 nautical-miles, thereby providing a significant relief from the standard 18% rate. However, vide NN.15/2025-CTR, the tax rate has been increased to 18% w.e.f. 22.09.2025.

Upon perusal of Para 25.1 to 25.2 of minutes of the 22<sup>nd</sup> GST Council, one can find the logic behind the change of rate on the aforesaid services from 18% to 12%. One of the reasons was the taxability of such services at 12% in the pre-GST regime. Further, the area beyond 12 nautical miles was beyond the jurisdiction of States, and therefore, VAT was not applicable, and only the Service Tax of 6% was charged. It was recommended to apply a tax rate of 12% instead of 18%. However, it seems that the new tax rate is contrary to the discussion held during the meeting.

With the offshore works contract services involving costly activities like construction and installation

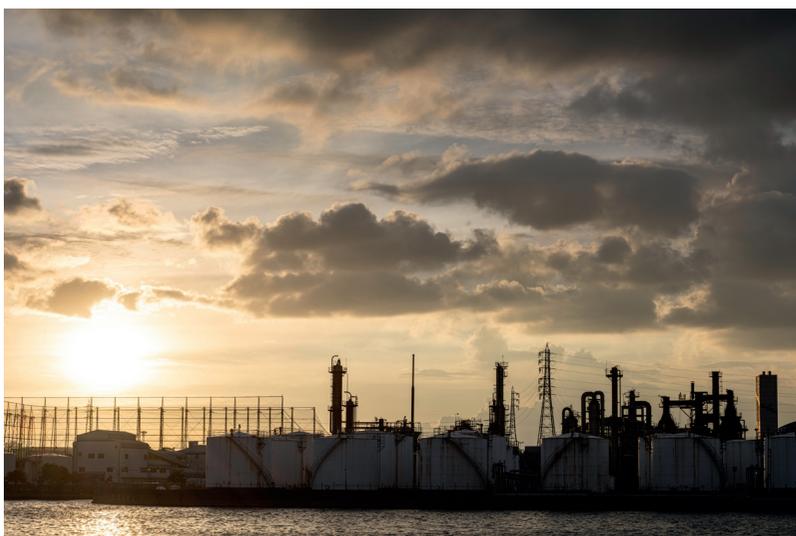
of wellhead platforms, derricks, etc, rather than shifting it to the 5% tax rate, the burden has been shifted onto the industry. The government must reconsider this, given petroleum's GST exclusion and the resulting cascading tax impact.

## iii. Support Services to the Industry

To facilitate operations across the upstream sectors, CBIC vide NN 20/2019- CTR introduced a 12% concessional rate for professional, technical and support services provided to the industry. However, the said rate has also been amended to 18% vide NN. 15/2025-CTR. One of the important concessions provided to the industry has now been snatched away. The government shall not just reconsider this decision but also provide clarity on the word "support services". At first glance, one might assume that all services in this industry qualify as "support services." However, Circular No. 114/33/2019-GST clarifies the services that can be brought under the umbrella to avail the concessional rate of tax. The circular provides two explanatory notes to determine the eligibility of services for the concessional benefit. Although the explanatory notes use the term 'includes' to define the list of services, the list itself is 'restrictive', thereby creating a dilemma for the industry. Misinterpretation has led to being prey of litigation and payment of taxes at a higher rate. CBIC should clarify the restriction or inclusiveness of the term "Includes" to avoid disputes.

## Recommendations

The exclusion of petroleum products from GST has sparked concerns due to its impact on production costs and consumer prices. The interplay of various taxes has increased the tax burden, while geopolitical factors further escalate production costs. Since fuel prices directly affect inflation and economic stability, government intervention often



“Excluding petroleum products is not just a taxation issue but an economic roadblock that increases costs and distorts market dynamics. Without GST, fuel prices remain artificially inflated due to multiple embedded taxes, ultimately increasing the costs of end products.”

prevents companies from transferring the full tax burden to consumers. Subsuming these taxes under GST could streamline the tax structure and reduce inefficiencies.

The 45<sup>th</sup> GST Council Meeting acknowledged the industry’s cost burden but deferred the proposal, citing that “this is not the right time to bring Petrol and Diesel within the ambit of GST.” The decision stems from the significant revenue reliance on petroleum products by both the central and certain state governments. Taxes on fuel have been a major source of revenue, which is why the Council would not bring it under GST. Further, the recent changes have pushed all the tax rates relevant to the industry into the 18% tax bracket, which further adds to their grievances. As GST is a destination-based tax, the inclusion would shift revenue from oil-producing states to

consuming states, creating concerns about revenue distribution. As per a report by Petroleum Planning and Analysis Cell (PPPAC), tax collected on petroleum products contributed Rs. 4,14,244 crore to the Central exchequer, whereas Rs. 3,25,583.5 crore to the State in F.Y. 2024-25. Additionally, the top-ranked states specifically with respect to revenue from taxes are provided in Table 2.

The revenue dynamics in the petroleum industry highlight a stark difference between state taxes on goods and GST collected on sales by the downstream industry. In the meantime, CBIC could provide the industry with temporary relief, discussion about which is as discussed below:

■ **Refund of Input Tax Credit**

The inclusion of petroleum products under GST is likely to take time as states work toward a consensus.

Meanwhile, what interim measures can the government implement to support the industry? Under Section 55 of the Act, the CBIC, through NN. 06/2017-CTR, granted a 50% refund of tax paid on all inward supplies of goods received by the Canteen Stores Department (hereinafter referred to as “CSD”) to compensate for the pre-GST exemptions and to ensure that essential goods remain affordable for the armed forces.

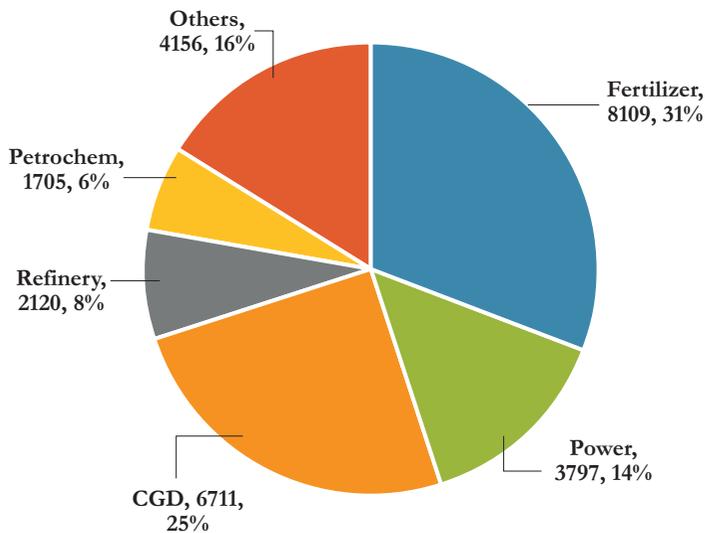
A similar approach could be applied to the industry. The government could identify key goods and services and introduce a partial refund mechanism, allowing businesses to claim refunds up to a specified limit.

A structured mechanism may also be instituted whereby a fixed percentage of the total input cost can be utilized against tax liabilities such as import

**Table 2**

State wise Collection of State Tax/VAT/GST on Petroleum, Oil and Lubricants				Amount in Crores
Sr. No	State	Sales Tax/VAT	SGST/UTGST	Total
1	Maharashtra	36,992.17	1653.9	38,646.07
2	Uttar Pradesh	31,214.11	909.72	32,123.83
3	Tamil Nadu	24,861.32	712.96	25,574.28
4	Gujarat	24,586.23	2980.24	27,566.47
5	Karnataka	23,427.58	410.09	23,837.67

### Natural Gas Sectoral Consumption Apr - Aug 2025



duties or excise duty on crude, similar to the duty credit framework presently extended to exporters.

#### ■ Shifting of tax rate for all goods and services

Currently, the GST rate of 18% applies to all necessary goods and services affecting not only companies but also consumers of petroleum products like diesel and petroleum. While other sectors received tax relief, the emerging oil and gas exploration industry is being ignored. It's crucial to address this by reducing the GST rate to 5% to stabilize the sector.

#### Conclusion

The industry constantly urges the ministries to include petroleum products into GST, but will this resolve all the issues? While to some extent, yes and to some, the issues still persist.

Excluding petroleum products is not just a taxation issue but an economic roadblock that increases costs and distorts market dynamics. Without GST, fuel prices remain artificially inflated due to multiple embedded taxes, which translates into increased costs for the end products. Integrating petroleum into GST would eliminate these inefficiencies and ensure a seamless credit mechanism in the supply chain.

A key justification for inclusion under GST is to utilize ITC, which is currently blocked, adding financial strain on the industry. Businesses could offset input taxes against output liability, reducing cascading effects. However, concerns remain that several critical inputs will still be ineligible for ITC under Section 17(5)(c) of the Act, as it disallows ITC on immovable property (except plant and machinery), impacting works contract services. Since "plant and machinery" excludes civil structures, ITC on infrastructure such as wellhead platforms may remain ineligible. While GST inclusion lowers tax costs, ITC restrictions will still inflate expenses, thereby raising consumer prices.

On the other hand, where petrol and diesel are taxed at approximately 42% and 34% of their final cost, respectively, alongside the imperative for states to sustain their revenue streams, if brought under GST, the rate would likely be no less than 28%.

Now, consider energy-intensive industries, particularly the fertilizer industry. According to an industry consumption report by the Petroleum Planning and Analysis Cell, the industrial sector, driven by the steel and cement industries, remains the largest energy

consumer of natural gas, by consuming 31% share between the period April 2025 to August 2025.

Also, the logistics and transport industry, where petroleum products constitute a major component of inputs and output services, capped at 5% or 18%, including petroleum under GST, would create an inverted duty structure, with input taxes exceeding the output taxes. This issue extends beyond transport and logistics to telecommunications, aviation, and other fuel-intensive industries. Further, with recent changes in the tax rates, the question of the inverted duty structure and refunds in relation to the same remains to be answered.

Additionally, the refund of ITC due to an inverted duty structure creates dual financial strain of reducing state revenue and an additional refund burden. CBIC must ensure inclusion is a comprehensive reform benefiting consumers, industries, and the economy.

Countries like New Zealand, Canada, and Saudi Arabia have successfully adopted a unified tax system for petroleum products. India, too, stands to gain from such a reform. The 55<sup>th</sup> GST Council meeting had initiated discussions on including natural gas, considering its role in fuel and fertilizers. However, prioritizing the inclusion of other petroleum products is equally essential. While concerns over revenue distribution persist, strategic and equitable tax allocation could address these challenges. The government must prioritize long-term economic stability over short-term revenue concerns. Delays in reform will hurt industrial competitiveness and global standing, while this reform is inevitable. It is now a question of when and how the government will make this historic transition.

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