

## Notes on recent oil price trends and VAT

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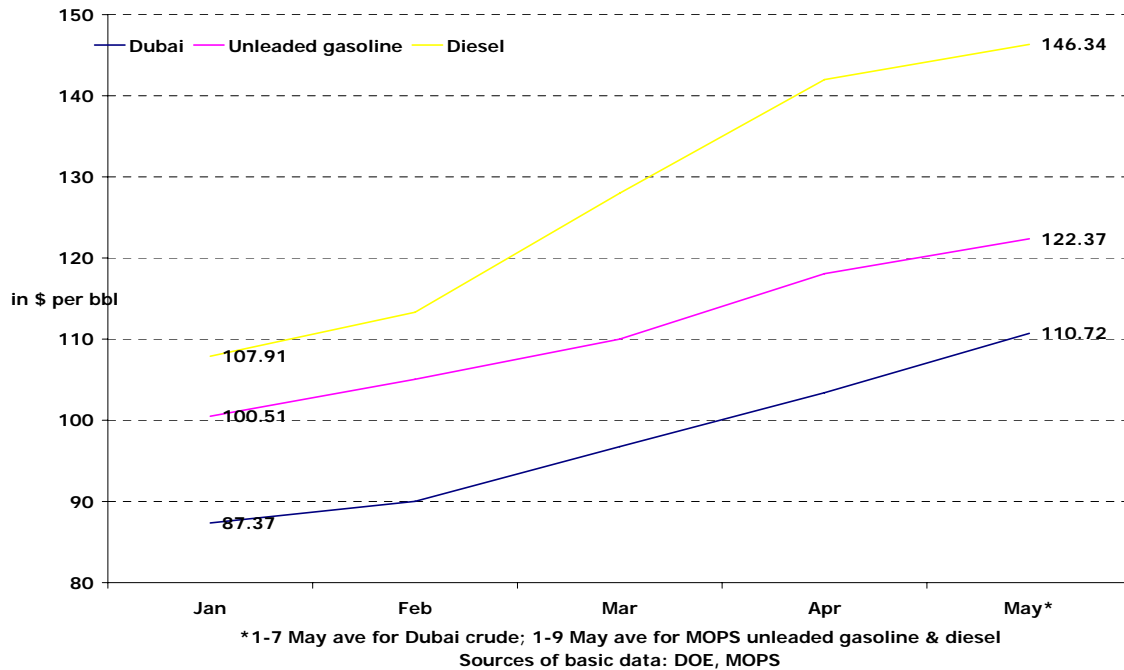
### Price movement

Oil companies, including the Big 3 (Petron, Shell and Chevron) claim that they use benchmark prices in the international oil market to determine domestic pump prices. For crude oil importers such as Petron and Shell, they refer to the Dubai crude spot price while other players that import refined petroleum products like Chevron refer to the Mean of Platt's Singapore (MOPS) spot prices.

The spot price of the benchmark Dubai crude is now pegged at \$110.72 per barrel as of the first seven days of May. It breached the \$100 a barrel monthly average in April and is now 26.7% higher than its average last January. On the other hand, MOPS-based unleaded gasoline averaged \$122.37 per barrel in the first nine days of May while diesel, \$146.34 per barrel. The said figures are 21.7% and 35.6% higher, respectively than their averages last January. (See **Chart 1**)

Chart 1

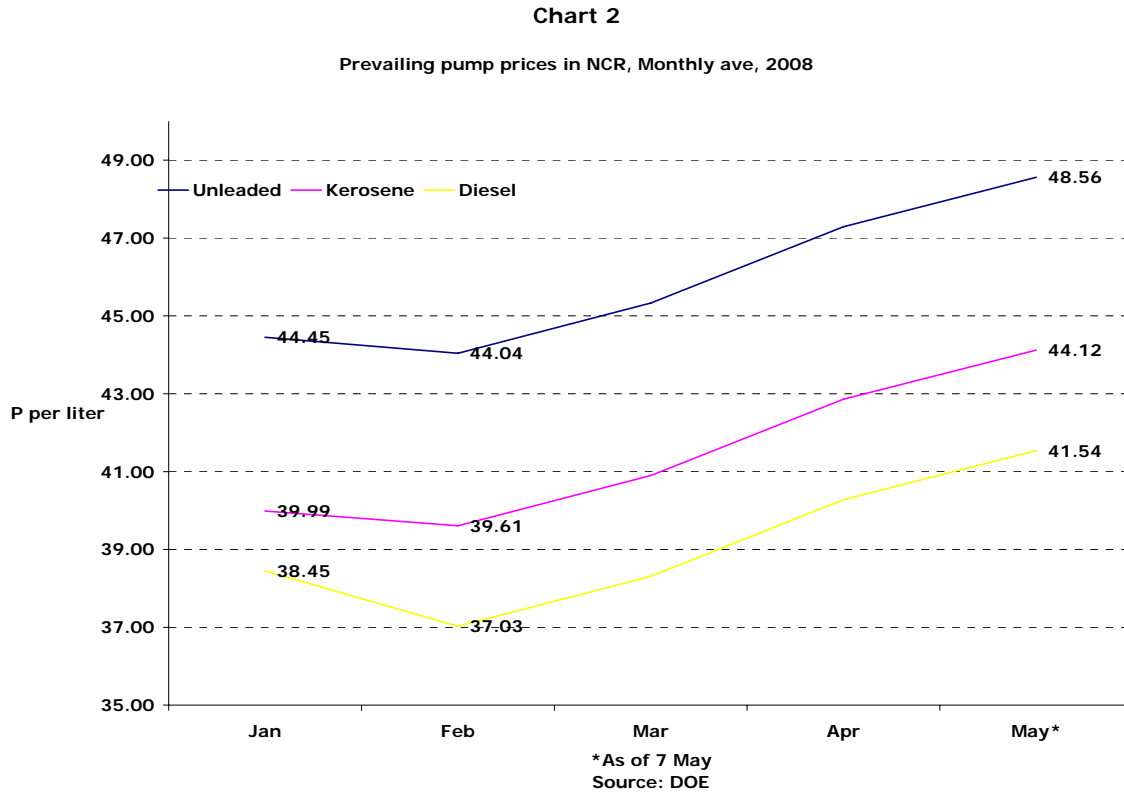
Monthly ave of Dubai crude & MOPS-based unleaded gasoline & diesel, 2008



Meanwhile, the country's foreign exchange has been declining since the start of the year with a 1-7 May average of P42.49 per US dollar, weaker by P1.59 from its January average.

These factors have supposedly combined to push domestic pump prices up. During the period in review, the prevailing pump price of unleaded gasoline in the National Capital Region (NCR) surged by P4.11 per liter between its January average and 1-7 May average; kerosene, by P4.13; and diesel, by P3.09. Overall, the average retail

price of various petroleum products increased by P3.58 per liter during the said period. (See **Chart 2**)



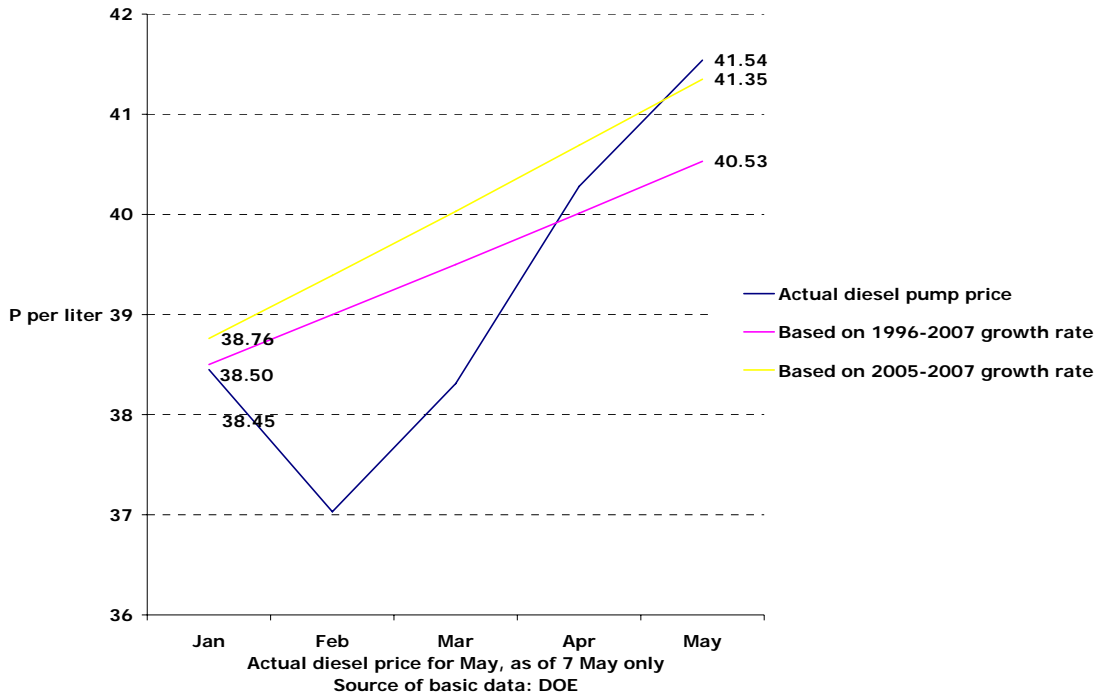
Domestic pump prices have increased much more rapidly this year than in the previous years. The prevailing price of diesel in NCR as 7 May, for example, has already exceeded Bayan's simulated monthly price for May 2008 based on the monthly average growth rate for 1996-2007 (deregulation period) and for 2005-2007. (See **Chart 3**) Note that the said prevailing price does not yet reflect the latest round (as of this writing) of P1 a liter oil price hike (OPH) implemented by the oil firms last 10 May. Five days before the said OPH round, Shell has warned that oil firms allegedly still need to recover P6-7 per liter more in the coming weeks.<sup>1</sup>

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<sup>1</sup> P6-7 fuel price increase seen, Philippine Daily Inquirer online, 6 May 2008

Chart 3

Actual pump price movement vs Bayan's simulated prices for diesel, 2008



Bayan has maintained that unmitigated price increases allowed under Republic Act (RA) 8479 or the Oil Deregulation Law of 1998<sup>2</sup> has only worsened the fundamental problem of transfer pricing by the global oil cartel and the speculative attacks by transnational banks and other giant financial firms that further artificially push oil prices up in the international market and taken advantage by the local Big 3 cartel (local units of the global cartel).<sup>3</sup>

Massive speculation, and not physical supply and demand balance, continues to account for recent global oil price surges with the Goldman Sachs predicting in May that prices could rise as high as \$200 a barrel over the next six months to two years.<sup>4</sup> One estimate claims that speculation now comprises as much as 60% of current global oil prices.<sup>5</sup>

### Token measures

Note that there was a general decline in domestic pump prices in February in spite of an uptrend in Dubai crude and MOPS spot prices apparently due to the Arroyo government's efforts to gain political points for the Energy Summit it organized from 29-31 January and 5 February. It was also the period that the clamor to scrap the

<sup>2</sup> RA 8479 is actually the second Oil Deregulation Law. The first, RA 8180, was passed in 1996 but was declared unconstitutional by the Supreme Court in 1997

<sup>3</sup> For further discussion, please refer to *Hinggil sa pagtaas ng presyo ng langis*, Bayan's powerpoint presentation downloadable from its website < <http://www.bayan.ph/> >

<sup>4</sup> Democrats: close speculation loophole, CNNMoney.com, 8 May 2008

<sup>5</sup> Perhaps 60% of today's oil is pure speculation by F. William Engdahl, Financial Sense Editorials, 2 May 2008

12% value added tax (VAT) on oil products to immediately lower pump prices started to gain ground.

To fend off criticisms that the Energy Summit does not offer anything concrete that could bring down pump prices as well as to derail the campaign to scrap the oil VAT, GMA rehashed the oil tariff adjustment mechanism through Executive Order (EO) 691.<sup>6</sup> Under this system, tariffs on imported crude oil and petroleum products will be reduced or waived based on certain trigger prices.<sup>7</sup> For February, GMA ordered a tariff cut of one percentage point.

Taking their cue from Malacañang, the biggest oil companies Petron and Shell implemented an oil price rollback of as much as P1 per liter starting 29 January and the other players followed suit.<sup>8</sup> But it has been a steep climb for domestic pump prices since then, starting with the 50 centavo a liter hike implemented by the oil firms on 1 March.

Overall, oil companies have implemented 10 rounds of oil price hikes that increased the pump prices of gasoline, kerosene and diesel by P6 per liter<sup>9</sup> between 1 March and 10 May, or an average of one OPH round per week. The biggest increases were implemented on 3 May and 10 May, when pump prices were raised by P1 per liter in each round from the usual 50 centavos a liter in the previous weekly increases.

The price increases since March has exposed the worthlessness of the oil tariff cut mechanism in lowering pump prices. For instance, the trigger price set by the Department of Finance (DOF) to reduce oil tariff from 3% to 0% for MOPS-based diesel is \$115.2 per barrel and \$103.25 per barrel for Dubai crude. Since March, MOPS-based diesel price has already breached the DOF trigger price and Dubai crude, since April. (See **Chart 4**) This means that the government is no longer collecting oil tariffs to supposedly mitigate domestic pump price increases but such intervention has not been felt at all.

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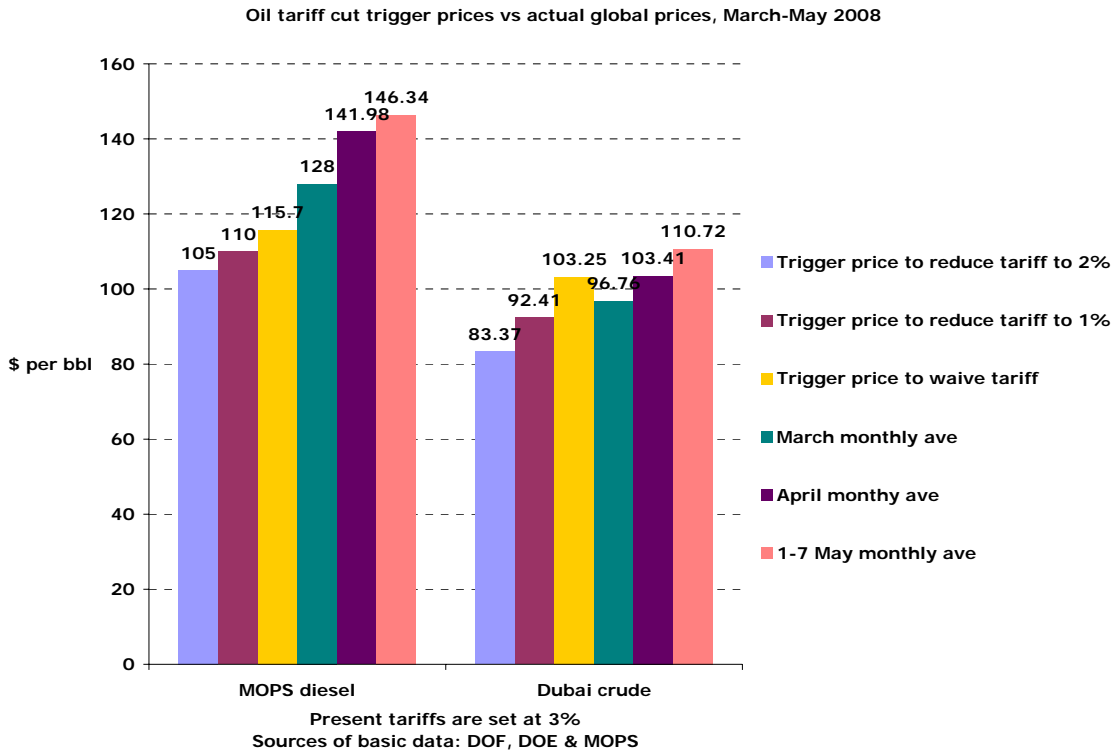
<sup>6</sup> EO 691 was signed by GMA on 10 January 2008

<sup>7</sup> Palace: no cut in VAT on oil, Philippine Daily Inquirer online, 15 January 2008

<sup>8</sup> (2<sup>nd</sup> update) Oil firms to cut prices by P1/liter, ABS-CBN news online, 29 January 2008

<sup>9</sup> Oil firms decide week not complete without price hike, Philippine Daily Inquirer online, 10 May 2008

Chart 4



In the face of more and bigger price hikes in the coming weeks, the Department of Energy (DOE) asked the oil firms to justify the increases but then later retreated to its usual helpless mode of pleading the oil companies to implement staggered increases. In response, Petron announced that it will revert to 50 centavo weekly price hikes until July to recover its supposed losses.<sup>10</sup> But note also that Petron made the announcement on the same day that the nationwide transport strike and people's protest against the oil VAT and the Oil Deregulation Law was held. Thus the announcement was an obvious, albeit meaningless, effort to appease the public.

### VAT cancellation

Meanwhile, the Arroyo government continues to ignore the demand to cancel the VAT on oil products as a doable measure to immediately bring down pump prices. The latest statement came from the DOF which argued that the "VAT on oil should be collected to fund the 2008 budget." Instead of oil VAT cancellation, the DOF is proposing to "use the revenues (from VAT) for targeted expenditures to cushion the impact of oil price hikes on the poorest of the poor."<sup>11</sup>

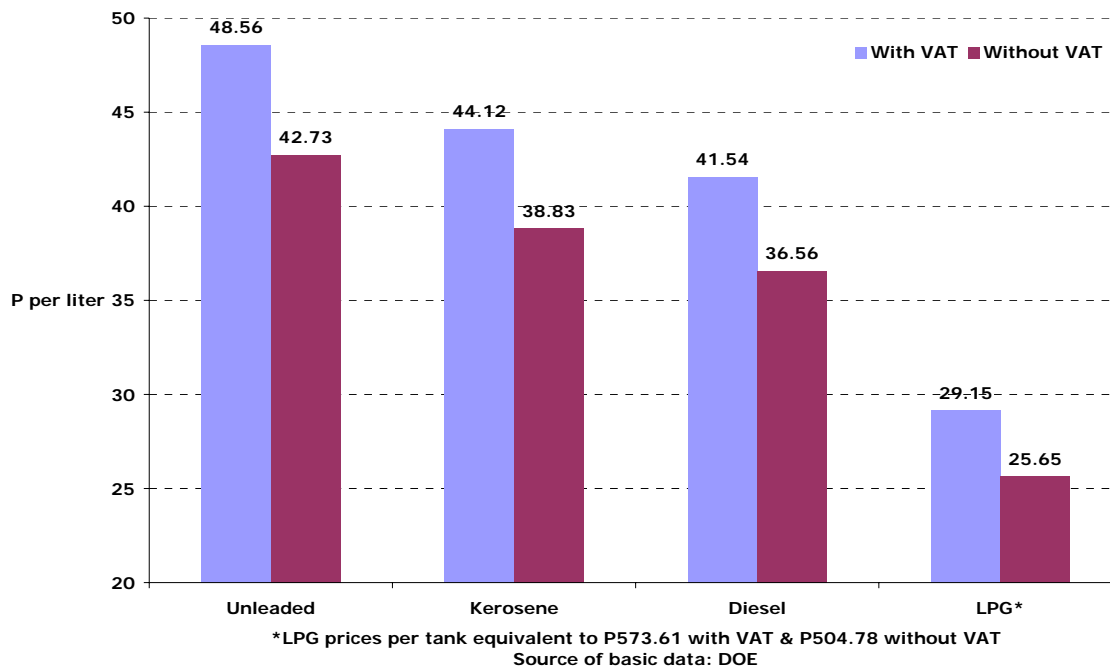
However, scrapping the VAT on oil remains the most immediately doable policy option which can significantly lower pump prices and provide relief to the consumers. Based on the prevailing prices in NCR as of 7 May, VAT cancellation can immediately bring down pump prices of unleaded gasoline by P5.83 per liter; kerosene, P5.29; diesel, P4.98; and liquefied petroleum gas (LPG), P68.83 per 11-kilogram cylinder tank. (See **Chart 5**)

<sup>10</sup> Major oil firm to revert fuel price hikes P0.50, Business World online, 13 May 2008

<sup>11</sup> DOF counts cost of suspending VAT on oil, Business World online, 13 May 2008

**Chart 5**

Comparative pump prices, with VAT & without VAT, as of 7 May 2008



In justifying the oil VAT, the DOF said that scrapping the said regressive tax will “bring minimal benefits to the lowest income groups.”<sup>12</sup> But Bayan has already pointed out the concrete and direct benefits that the poor will reap from the oil VAT cancellation, including the jeepney and tricycle drivers, small fishers, and poor households using kerosene and LPG. (See **Table 1**)

**Table 1**

Estimated benefits of oil VAT cancellation based on 7 May 2008 prevailing prices in NCR				
Sector	How much do they spend on oil?		How much will they save without the oil VAT?	How many will benefit? (nationwide)
	With VAT	Without VAT		
Jeepney drivers using 30 liters of diesel per daily trip	P1,246.20 per daily trip	P1,096.66 per daily trip	P149.54 per daily trip	426,572 jeepney drivers
Tricycle drivers using 4 liters of unleaded gasoline per daily trip	P194.24 per daily trip	P170.93 per daily trip	P23.21 per daily trip	581,578 tricycle drivers

<sup>12</sup> *ibid*

Small fishers using motorized bancas with 10 liters of regular gasoline per fishing trip	P458.60 per fishing trip	P403.57 per fishing trip	P55.03 per fishing trip	708,000 small fishers
Households using 11-kg LPG tank	P573.61 per tank	P504.78 per tank	P68.63 per tank	8.6 million households
Households using 4.2 liters of kerosene per month for lighting & cooking	P185.30 per month	P163.07 per month	P22.24 per month	9.4 million households
Sources of basic data: DOE, LTO, IMF, NSO, Piston, Pamalakaya, interviews				

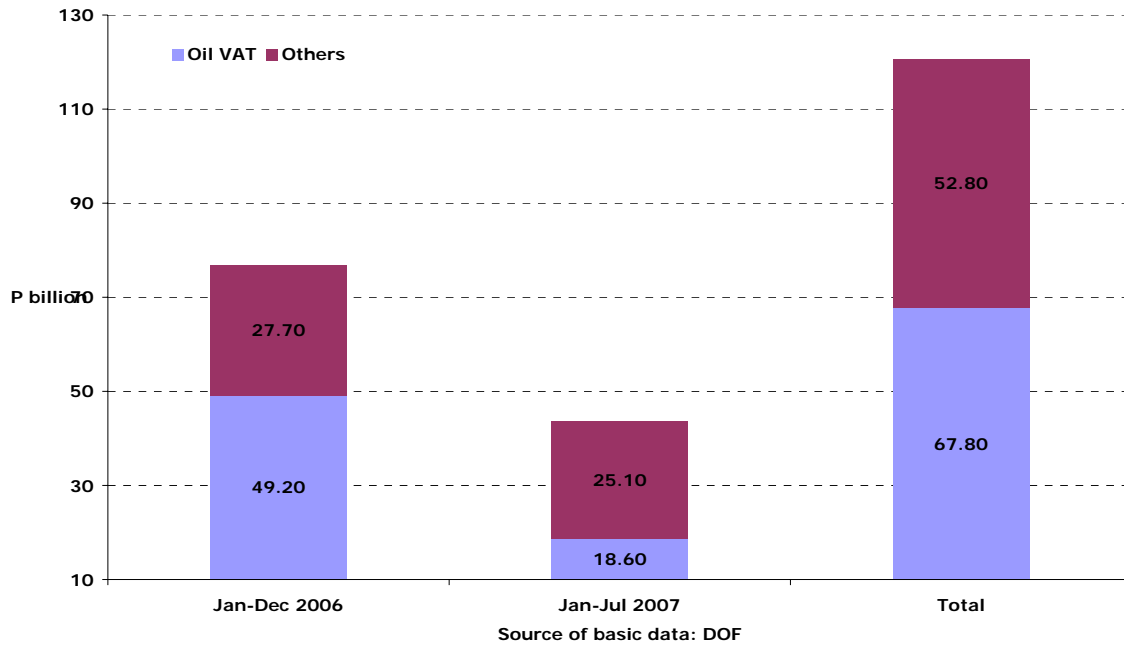
The real reason behind Malacañang's persistent refusal to scrap the oil VAT is its impact on the national budget deficit that could affect the regime's foreign borrowings. The oil VAT provides a steady stream of revenues for the government, especially amidst high oil prices, which is favorable for the country's credit worthiness. The DOF estimated that removing the VAT on oil products will result in P54 billion annual revenue losses<sup>13</sup> for the national government. DOF data also show that the oil VAT accounted for 56.2% of total VAT revenues raised by the GMA regime from 2006 to the first half of 2007.<sup>14</sup> (See **Chart 6**)

<sup>13</sup> Sen. Roxas, on the other hand, claims that net yearly revenue losses if the oil VAT is removed is only around P30 billion because the amount saved by consumers from the VAT removal can be translated to increased consumption of other VAT-able goods and services.

<sup>14</sup> There is no available data yet on full-year VAT collections for 2007 showing revenues from the oil VAT. Latest data from the Bureau of Treasury peg total VAT revenues at P69.47 billion from January to September 2007.

Chart 6

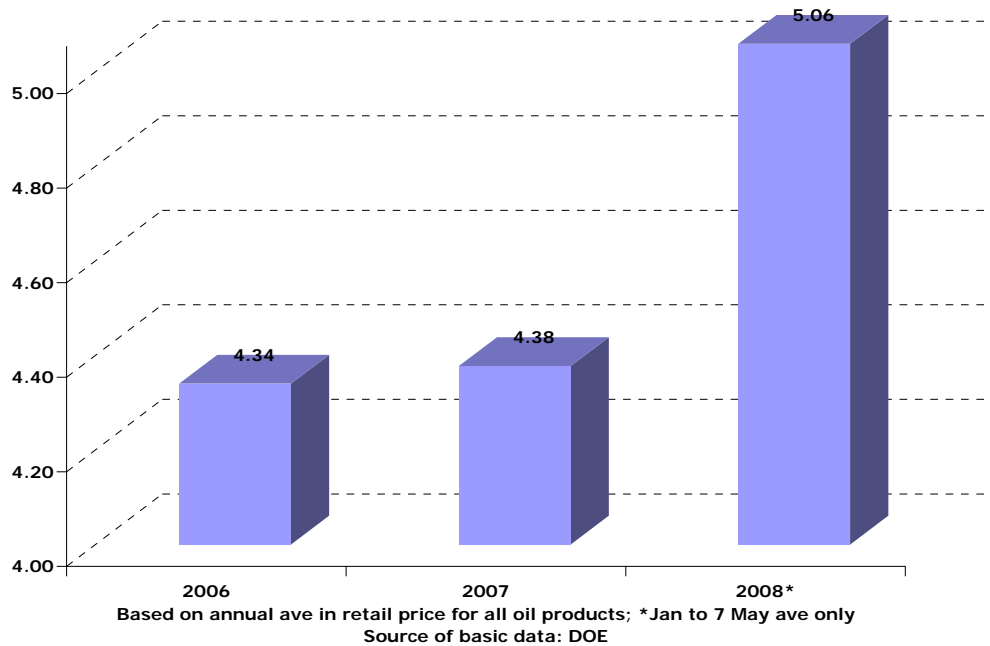
NG VAT collections from oil & others, 2006 & 1st sem 2007



Higher oil prices mean more revenues for the GMA regime that will assure its foreign creditors of debt repayments. In 2006, for example, Bayan estimates show that the government collected an average of P4.34 per liter in VAT for all petroleum products. This year, it is collecting 72 centavos per liter more in oil VAT due to unabated price increases. (See **Chart 7**)

Chart 7

Estimated VAT collections per liter from all petroleum products



The regime's so-called fiscal health should take a backseat to the more pressing problem of the ordinary people on high and increasing oil prices. In the first place, the government is raising revenues to supposedly help ease the people's burden – a responsibility that it has not been fulfilling as most revenues go to debt servicing and lost to corruption. Cancelling the oil VAT thus simply means returning back the people's money which will translate to actual, immediate and direct benefits (in the form of lower oil prices and improved incomes) instead of entrusting that money to a corrupt and anti-poor regime through the oil VAT.

Furthermore, even if the oil VAT is removed, there are other measures that government can do to raise revenues. Tax effort, for instance is dismal – in 2007, tax effort was only 10.3%, a significant drop from 2006's 14.3 percent. Certainly, improving efficiency in tax collections will result in billions of pesos in additional revenues. Addressing bureaucratic corruption can raise revenues as well as an estimated P30 billion in public funds are lost annually due anomalous contracts alone such as the NBN-ZTE scam.<sup>15</sup> Tax perks and fiscal incentives to big foreign corporations and the liberalization of trade have also resulted in billions of pesos in foregone revenues and these policies must be reversed.

At present, there are two bills pending at the Senate that seek to suspend or scrap the oil VAT. Senate Bill (SB) 1962 filed by Senator Mar Roxas proposes to suspend the imposition of the oil VAT for six months. SB 1977 of Senator Miguel Zubiri, on the other hand, offers to exempt petroleum products (as well as electricity) from the VAT.<sup>16</sup> SB 1962 and SB 1977 have been pending at the ways and means committee

<sup>15</sup> Corruption, inefficiency cost govt P30B yearly, Manila Times internet edition, 4 April 2008

<sup>16</sup> Addressing the oil price increase, Senate Economic Planning Office policy brief, January 2008

of the Senate since December 2007. At the House of Representatives, the Gabriela Women's Party (GWP) has filed House Bill (HB) 3442 to cancel the VAT on petroleum products but has yet to be scheduled for first reading.