Essar Oil Limited

16th Annual Report 2005-2006

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BOARD OF DIRECTORS (As on 28th August, 2006)

Shashi Ruia	*Chairman*
Ravi Ruia	*Vice Chairman*
Prashant Ruia	
Anshuman Ruia	
Awadhesh N. Sinha	*Managing Director & CEO*
Hari L. Mundra	*Dy. Managing Director & Director (Finance)*
Suresh Mathur	*Wholetime Director*
Dilip J. Thakkar	
K. N. Venkatasubramanian	
Dr. G. Goswami	*Nominee of IDBI Ltd.*
N.S. Kannan	*Nominee of ICICI Bank Ltd.*
Sanjeev Ghai	*Nominee of IFCI Ltd.*

COMPANY SECRETARY

Sheikh S Shaffi

BANKERS

ICICI Bank Ltd.
State Bank of India
Punjab National Bank
IDBI Bank Ltd.
Central Bank of India
State Bank of Saurashtra
Indian Overseas Bank
HDFC Bank Ltd.
Oriental Bank of Commerce
Allahabad Bank

AUDITORS

M/s. Deloitte Haskins & Sells
Chartered Accountants
12, Dr. Annie Besant Road
Opp. Shiv Sagar Estate, Worli
Mumbai – 400 018

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REGISTERED OFFICE

Khambhalia Post, Post Box No. 24
Dist. Jamnagar - 361 305, Gujarat
Tel.: 02833 - 241444
Fax: 02833-241616 / 241414

CORPORATE OFFICE

Essar House
Post Box No. 7945
11, Keshavrao Khadye Marg,
Mahalaxmi, Mumbai - 400 034
Tel.: 022-66601100 Fax : 022-24954281
Website : http://www.essar.com

TRANSFER AGENTS

M/s. Sharepro Services (India) Pvt. Ltd.
Unit: Essar Oil Limited
Satam Estate, 3rd Floor
Above Bank of Baroda
Cardinal Gracious Road
Chakala, Andheri (East)
Mumbai - 400 099
Tel.: 022-28215168
Fax: 022-28375646
Email: sharepro@vsnl.com
Website:http://www.shareproservices.com

SHARES LISTED AT

Bombay Stock Exchange Ltd.	1st Floor, Rotunda Bldg., P.J. Towers Dalal Street, Mumbai - 400 023
National Stock Exchange of India Ltd.	Exchange Plaza, 5th Floor, Plot No. C/1 G Block, Bandra-Kurla Complex Bandra (E), Mumbai - 400 051
*The Calcutta Stock Exchange Association Ltd.	7, Lyons Range, Kolkata - 700 001

*(Applied for delisting)

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NOTICE

NOTICE is hereby given that the **Sixteenth Annual General Meeting** of the members of **ESSAR OIL LIMITED** will be held at the Registered Office of the Company at Khambhalia Post, (40th Km. stone on Jamnagar-Okha Highway) Dist. Jamnagar - 361305, Gujarat on **Friday** the **29th September, 2006** at **2:30 p.m.** to transact, with or without modifications, as may be permissible, the following business:

ORDINARY BUSINESS:

1. To receive, consider, approve and adopt the Balance Sheet as at 31st March, 2006, the Profit & Loss Account for the financial year ended on that date and the reports of the Board of Directors and Auditors thereon.
2. To appoint a Director in place of Shri Shashikant N Ruia who retires from office by rotation and being eligible, offers himself for reappointment.
3. To appoint a Director in place of Shri Dilip J Thakkar who retires from office by rotation and being eligible offers himself for reappointment.
4. To appoint M/s. Deloitte Haskins & Sells, Chartered Accountants, Mumbai, as Auditors to hold office from the conclusion of this Annual General Meeting until the conclusion of the next Annual General Meeting and to authorise the Board of Directors to fix their remuneration.

SPECIAL BUSINESS:

5. To consider and, if thought fit, to pass the following resolution as an Ordinary Resolution:

   "RESOLVED THAT Shri Anshuman S Ruia, who was appointed as an Additional Director by the Board of Directors pursuant to section 260 of the Companies Act, 1956 and who holds office upto the date of this Annual General Meeting and in respect of whom the Company has received a notice under section 257 of the Companies Act, 1956, in writing, proposing his candidature for the office of director, be and is hereby appointed as a Director of the Company liable to retirement by rotation."
6. To consider and, if thought fit, to pass the following resolution as an Ordinary Resolution:

   "RESOLVED THAT Shri Suresh C Mathur, who was appointed as an Additional Director by the Board of Directors pursuant to section 260 of the Companies Act, 1956 and who holds office upto the date of this Annual General Meeting and in respect of whom the Company has received a notice under section 257 of the Companies Act, 1956, in writing, proposing his candidature for the office of director, be and is hereby appointed as a Director of the Company liable to retirement by rotation."
7. To consider and, if thought fit, to pass the following resolution as a Special Resolution:

   "RESOLVED THAT pursuant to the provisions of sections 198, 269, 309 and other applicable provisions, if any, of the Companies Act, 1956 read with Schedule XIII thereto, and subject to such approval(s) from the Central Government or any other authority, as may be required, and subject to any conditions and / or modifications as may be imposed and / or suggested by such authorities, while granting such approvals, approval of the Company be and is hereby given to the appointment of Shri Suresh C Mathur as Wholetime Director of the Company with effect from 4th April, 2006 upto 31st August, 2008, determinable earlier at the option of the Board of Directors (which term shall include the Remuneration Committee constituted by the Board of Directors) and for payment of remuneration during his tenure in office as Wholetime Director upon the terms and conditions as set out in the Explanatory Statement annexed to this Notice which is hereby specifically approved with authority to the Board of Directors to alter and vary the terms and conditions as may be agreed to between the Board of Directors and Shri Suresh C Mathur, in the best interest of the Company."

   "RESOLVED FURTHER THAT the Board of Directors be and is hereby authorised to take such steps as may be necessary or expedient to give effect to this resolution."

By Order of the Board of Directors

Mumbai
28th August, 2006

SHEIKH S. SHAFFI
Company Secretary

Registered Office:
Khambhalia Post, P. O. Box 24,
Dist. Jamnagar-361 305, Gujarat

NOTES:

1. **A member entitled to attend and vote at the meeting is entitled to appoint a proxy to attend and vote instead of himself and the proxy need not be a member of the Company. The proxy, in order to be effective, must be deposited at the Registered Office of the Company not less than 48 hours before the commencement of the meeting.**
2. The Register of Members and Share Transfer Books of the Company will remain closed from Thursday, the 28th day of September, 2006 to Saturday, the 30th day of September, 2006 (both days inclusive).
3. All documents referred to in the accompanying Notice are open for inspection at the Registered Office of the Company on all working days, except Saturdays, Sundays and Bank holidays, between 11:00 a.m. and 1:00 p.m. upto the date of the Annual General Meeting.
4. Members / proxies should bring the attendance slip duly filled in for attending the meeting.
5. Members desiring any information with regard to Accounts / Reports are requested to write to the Company at least ten days before the date of the meeting, so as to enable the management to keep the information ready.

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6. Directors retiring by rotation:

   Shri Shashikant N Ruia, Chairman of Essar Group is a well known industrialist of India. He is 62 years old. As an entrepreneur he has enabled the Essar Group to gain a premier position amongst industrial houses in India within a span of two decades. Shri S N Ruia began his career in his family business under the guidance of his father, late Shri Nand Kishore Ruia, in 1969. Owing to Shri S N Ruia's alacrity and indomitable passion, the Group has forayed into areas which were the exclusive preserve of either multinational giants or the Indian public sector such as Steel, Oil Exploration, Refining & Retailing, Power, Telecom, Shipping, Marine Constructions and Offshore Engineering. The other companies in which Shri S N Ruia is a Director are: Essar Shipping Ltd.; Essar Steel Ltd.; Essar Power Ltd.; Essar Constructions Ltd.; India Securities Ltd.; Vadinar Oil Terminal Ltd.; Hazira Steel Ltd.; Hazira Plate Ltd. and Essar Steel (Hazira) Ltd. He does not hold any shares in the Company. Shri S N Ruia retires by rotation at the Annual General Meeting and offers himself for reappointment.

   Shri Dilip J Thakkar is 69 years old. He is a practicing Chartered Accountant with 45 years experience in Taxation and FEMA matters. The other companies in which Shri Dilip J Thakkar is a Director are: Blueberry Trading Company Pvt. Ltd.; Chrysanthemum Investments Pvt. Ltd.; Deccan Florabase Ltd.; Hamlet Constructions India (P) Ltd.; Himatsingka Seide Ltd.; Indo Count Industries Ltd.; Panasonic Battery India Co. Ltd.; Wearology Ltd.; Omega Management Services Ltd.; PAE Ltd.; Rajasvi Properties Holdings Pvt. Ltd.; Starrock Investments & Trading Pvt. Ltd.; The Ruby Mills Ltd.; Thirumalai Chemicals Ltd.; Township Real Estate Developers Pvt. Ltd.; Walchandnagar Industries Ltd. and Windmere Hospitality (I) Pvt. Ltd. He is also Chairman of the Audit & Governance Committee and member of Investors' Relations Committee of the Board. He holds 300 shares in the Company. Shri Dilip J Thakkar, retires by rotation at the Annual General Meeting and offers himself for reappointment.

7. The Explanatory Statements pursuant to section 173(2) of the Companies Act, 1956 relating to the Special Business mentioned in Item Nos. 5 to 7 of the accompanying Notice are annexed.

ANNEXURE TO NOTICE

Explanatory Statements pursuant to section 173(2) of the Companies Act, 1956

Item No. 5

Shri Anshuman S Ruia, Promoter Nominee, was appointed as an Additional Director of the Company on 30th September, 2005. In terms of section 260 of the Companies Act, 1956 and Articles 82 of Articles of Association of the Company Shri A S Ruia would hold office as a Director upto the date of the ensuing Annual General Meeting.

Shri A S Ruia is 35 years old. He is the younger son of the Chairman of Essar Group, Shri S N Ruia and has over a decade's experience covering the Group's major businesses and currently looks after the Power and Telecom businesses. Shri A S Ruia is also involved in new business ventures and I.T. activities of the Group. In addition, he also works on consolidation of the Group's business enterprises and strategy for growth. He is a Director on Essar Power Ltd.; Vadinar Power Company Ltd.; India Securities Ltd.; Essar Shipping Ltd.; Vadinar Oil Terminal Ltd.; Hutchison Essar Ltd.; BPL Mobile Communications Ltd.; Essar Power M P Ltd.; Aegis BPO Services Ltd. and Essar Power Transmission Company Ltd. He does not hold any shares in the Company.

The Directors recommend the resolution at Item No. 5 of the Notice for your approval.

Shri S N Ruia, Shri R N Ruia and Shri P S Ruia may be treated as interested in the resolution. None of the other directors is concerned or interested in the resolution at Item no. 5.

Item Nos. 6 and 7

Shri Suresh C Mathur was appointed as Additional Director and thereafter as Wholetime Director of the Company w.e.f. 4th April, 2006 to hold office upto 31st August, 2008.

In terms of section 260 of the Companies Act, 1956 (Act) and Article 82 of Articles of Association of the Company, Shri Suresh C Mathur would hold office as a Director upto the date of the ensuing Annual General Meeting. Accordingly, the resolution at item no. 6 of the Notice is being proposed for his appointment as Director of the Company.

At the time of appointment of Shri Suresh C Mathur, as per the audited Balance Sheet for the financial year (15 months) ended 31st March, 2005 (2004-2005), the profits of the Company were inadequate under the provisions of section 198 read with sections 309, 349 and 350 of the Act for payment of remuneration to the managerial personnel. Accordingly, in terms of sections 269, 198 and other applicable provisions of the Act, the Company has made application to the Central Government on 30th June, 2006 for appointment of and payment of remuneration to Shri Suresh C Mathur as Wholetime Director.

Further, as per the audited Balance Sheet for the financial year ended on 31st March, 2006, the Company has no profits. Accordingly, approval of the members at General Meeting is required in terms of sections 269 and 198(4) read with Schedule XIII of the Act for appointment of Shri Suresh C Mathur as Wholetime Director and payment of managerial remuneration to him for his tenure in office.

Shri Suresh C Mathur is a Director of Gujarat State Petroleum Corporation Ltd. and Gujarat State Petronet Ltd. He does not hold any shares in the Company.

Information required to be given to members as per Schedule XIII of the Companies Act, 1956 is as under:

I General Information:

The Company belongs to the oil and gas industry. It is an existing Company engaged in exploration and production of oil and gas and marketing of petroleum products and is setting up an oil refinery at Vadinar, Dist. Jamnagar, Gujarat, with a capacity of processing 10.5 million metric tons per annum crude oil (Refinery project). The Refinery project is

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under implementation and has not yet commenced commercial production. The work at the Refinery project was affected due to a severe cyclone in June 1998, causing delay in project implementation and consequent delay in restart of the project. A debt restructuring package was approved by the Empowered Group of the Corporate Debt Restructuring (CDR) Cell of lenders. Additional funds were raised by issue of Foreign Currency Convertible Bonds (FCCBs) aggregating to US$ 207 million (which have since been converted into Global Depository Shares) and the lenders have disbursed additional funds. The Company restarted project construction activities in January, 2005. The Company is likely to commence the first phase of production in October, 2006.

Essar Energy Holdings Ltd. (formerly Prime Finance Company Ltd.), Foreign Co-Promoter, has made investment of Rs.252 Crore in the Company and presently holds 4,63,29,290 (4.28%) equity shares of the Company.

The financial performance of the Company in the past five years was as under:

(Rs. in crore)

Financial parameters	Year				
	2000-2001	2001-2002	2002-2003	2004-2005	2005-2006
	(12 months period ended on 31/3/2001)	(18 months period ended on 30/9/2002)	(15 months period ended on 31/12/2003)	(15 months period ended on 31/3/2005)	(12 months period ended on 31/3/2006)
Turnover	167.94	292.64	173.25	1045.12	636.63
Net profit (as computed under section 198)	13.91	44.47	22.19	16.82	(112.39)
Net profit as per Profit & Loss account	10.43	25.16	20.64	9.86	(93.68)

II Information about Shri Suresh C Mathur:

Shri Suresh C Mathur is 66 years old. He has varied experience of over 40 years in the Oil Industry. He is a Chartered Accountant by qualification. He has held important assignments in the field of Finance, Marketing, Operations, Strategic Planning, International Oil Trading, and execution of several Projects. Prior to joining Essar Group, Shri Mathur was the CEO & Managing Director of Petronet LNG Limited which under his leadership set up India's first LNG import and regasification terminal of 5 MMTPA capacity at West Coast of India in Dahej. He also initiated the process of doubling the Dahej's terminal capacity to 10 MMTPA besides setting up its second terminal in South West India at Kochi. He was the Finance Director of IOC, prior to taking over the charge of Petronet LNG Limited. He also headed IOC's International Trade responsibility for procurement of Crude Oil & Petroleum Products for the country, as IOC was the Governments Canalizing Agency for imports of crude oil and petroleum products. Shri Mathur has served ITC, Geneva and World Bank as Consultant and has authored a book for them on "Handbook for Import of Crude Oil & Petroleum Products for developing Countries". Shri Mathur served on a World Bank Project in Nigeria for 3 years (1979-1981).

Shri Mathur has been awarded Chemtech Foundation Award under Leadership & Excellence Series as "Achiever of the Year" Natural Gas Category by Governor of Maharastra for pioneering the implementation of World Class LNG infrastructure in the country. The President of French Republic, Mr. Jacques Chirac has conferred the country's second highest civilian honor 'Knight of the Order of Merit' to Shri Mathur in recognition of his leadership and professional acumen in development of the country's first LNG import terminal at Dahej.

Shri Suresh C Mathur will be responsible for handling International Trading operations of Oil & Gas and has extensive experience in the field as stated above. With the Refinery to be commissioned shortly, the Company will be procuring / importing crude oil and exporting petroleum products internationally, a very important function for the refinery. Shri Suresh C Mathur with his expertise is considered well suited to handle this challenging responsibility.

Before joining the Company, Shri Suresh C Mathur was working with Petronet LNG Limited as its CEO & Managing Director till July, 2006 and thereafter with Essar Steel Limited. During the financial year 2005-2006 he earned a consolidated remuneration of Rs. 72.39 lakhs. The remuneration proposed to be paid to the Wholetime Director is comparable with the remuneration being paid for similar assignments in the industry.

The particulars of remuneration payable and the terms of the appointment of Shri Suresh C Mathur are basic salary of Rs. 1,00,000 per month in the scale of Rs. 1,00,000 – Rs. 2,00,000 per month, as may be determined by the Board or the Remuneration Committee constituted by the Board. In addition to the salary, the Wholetime Director shall be entitled to allowances namely House Rent Allowance and special allowance aggregating to Rs. 5,00,000 per month at present. He shall be entitled to provision of Company car and full reimbursement of car expenses. Further, he may be entitled for telephone expenses, entertainment expenses incurred for Company's business, full reimbursement of domiciliary medical expenses incurred for him, his spouse and dependent children and hospitalisation facilities as per the Company's Hospitalisation scheme, performance bonus as may be determined by the Board. The perquisite value of the facilities / benefits / allowances and bonus shall be evaluated, wherever applicable, as per the Income Tax Act, 1961 and the Rules framed thereunder. However, the total of salary / perquisites / allowances / other benefits and bonus as may be decided by the Board of Directors or the Remuneration Committee, will not exceed Rs.10,00,000 per month.

The Wholetime Director shall not be entitled, under any circumstances whatsoever, to any compensation for loss of office, unless otherwise decided by the Company.

In the event of loss or inadequacy of profits in any financial

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year during the period of appointment, the remuneration payable as aforesaid, will be paid as minimum remuneration subject to the approval of Central Government, as may be required.

Shri Suresh C Mathur does not have direct or indirect pecuniary relationship with the Company or relationship with the managerial personnel other than getting remuneration as the Wholetime Director of the Company.

The above may be treated as an abstract of the agreement between the Company and Shri Suresh C Mathur pursuant to section 302 of the Act.

III Other information:

(1) Reasons for loss / inadequacy of profit, if any.

There were losses during the financial year ended 31st March, 2006, because of the following reasons:

i. The Company in 2003 started trading of petroleum products through retail outlets set up on franchisee basis and also through direct sales to bulk customers as seeding operation and as a precursor to its own refinery production. During the financial year ended 31st March, 2006, the Company generated a turnover of Rs. 636.63 crore from sales of petroleum products. The Company incurred losses on account of unprecedented rise of crude oil prices in the International market resulting in increase of procurement prices of petroleum products while retailing prices have been controlled by Central Government and have not been correspondingly increased. This has had a direct negative impact on the margins. Income and profits from the trading operations depends on the selling prices of petroleum products fixed by Central Government.

ii. The Refinery project of the Company is still under implementation and the benefits to arise from its commercial operation are not yet available to the Company.

iii. The Drilling division, the main source of income and profit, was sold in May 2003 to comply with the pre disbursement conditions by the lenders to the Refinery Project and the sale proceeds were brought in to part finance the cost of the Refinery Project.

(2) Steps taken or proposed to be taken for improvement.

The Company has already restarted work at the refinery project site. A workforce of over 15000 persons has been mobilized at the project site and overall project completion as of 31st March, 2006 is 85.5%. The Company is likely to commence the first phase of production in October, 2006.

(3) Expected increase in profitability and profits in reasonable terms.

After commissioning of the full Refinery in April 2007, the first full year of operation is expected to generate a turnover of about Rs. 17,500 crore and net profit of about Rs. 500 crore.

The Board of Directors is of the opinion that the appointment of Shri Suresh C Mathur as Wholetime Director and payment of the proposed remuneration to him would be in the interest of your Company. Directors accordingly recommend the resolution at Item No. 7 of the Notice for your approval.

None of the other Directors is concerned or interested in the resolutions at Item nos. 6 and 7 except for Shri Suresh C Mathur.

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By Order of the Board of Directors

Mumbai
28th August, 2006

SHEIKH S. SHAFFI
Company Secretary

Registered Office:
Khambhalia Post, P. O. Box 24,
Dist. Jamnagar-361 305, Gujarat

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DIRECTORS' REPORT

To the Members of Essar Oil Limited

Your Directors have pleasure in presenting the Sixteenth Annual Report together with the audited accounts of the Company for the financial year ended March 31, 2006.

FINANCIAL RESULTS

(Rs. in crore)

	2005-2006 (12 months)	2004-2005 (15 months)
Gross Income	699.22	1146.58
Gross Profit / (Loss)	(87.39)	20.58
Less: Depreciation	4.66	6.22
Profit / (Loss) before Income Tax	(92.05)	14.36
Less: Provision for Income Tax / Deferred Tax Liability / Fringe Benefit Tax	1.63	4.50
Net Profit / (Loss)	(93.68)	9.86
Add: Balance brought forward from previous year	82.89	82.89
Add: Transfer from Foreign Project Reserve	18.50	—
Total amount available for appropriations	7.71	92.75
Less: Appropriations		
(a) Foreign Projects Reserve	—	—
(b) Debenture Redemption Reserve	—	9.86
(c) Transfer to General Reserve	—	—
(d) Proposed Dividend	—	—
Balance to be carried to Balance Sheet	7.71	82.89

INCREASE IN THE SHARE CAPITAL

During the year, the paid up capital of the Company increased from 93,92,98,314 equity shares of Rs.10/- each to 108,35,77,314 equity shares of Rs.10/- each upon issue of 14,42,79,000 equity shares of Rs.10/- each to the overseas depository for Global Depository Shares (GDS) upon exercise of option by holders of FCCBs aggregating to US$ 41 Million to convert their holdings into GDS.

Pursuant to approval granted by the shareholders at the 15th Annual General Meeting held on 30th September, 2005, the Company has proposed to issue GDSs aggregating to US$ 78 million to Promoters on preferential issue basis. In-principle approvals of National Stock Exchange of India Ltd. and Bombay Stock Exchange Ltd. for listing of the shares represented by the GDS have been obtained. The securities will be allotted shortly.

INFORMATION ON STATUS OF COMPANY'S AFFAIRS

Information on operational and financial performance, status of construction activities at project site, etc. is given in the Management Discussion and Analysis which is annexed to the Directors' Report and has been prepared in compliance with the terms of clause 49 of the Listing Agreement with Indian Stock Exchanges.

DIRECTORS

During the year Shri Anshuman S Ruia joined the Board as Additional Director and Shri Suresh Mathur was appointed as Wholetime Director effective from 4th April, 2006. Shri Sanjeev Ghai was appointed as Nominee Director of IFCI Ltd. in place of Shri Sanjoy Chowdhury. In September, 2005, Shri K Sridhar was nominated by Life Insurance Corporation of India and subsequently he resigned in June 2006. Shri S N Gogate, Nominee of the Debenture Trustees, The Western India and Trustee Executor Company Ltd. also resigned in July 2006.

The Board wishes to place on record its appreciation for the valuable services rendered by Shri Sanjoy Chowdhury, Shri K Sridhar and Shri S N Gogate during their tenure as members on the Board.

Shri Shashikant N Ruia and Shri D J Thakkar retire by rotation at the ensuing Annual General Meeting and offer themselves for re-appointment.

DIRECTORS' RESPONSIBILITY STATEMENT

Pursuant to the provisions of section 217(2AA) of the Companies Act, 1956, it is hereby confirmed:

(i) that in the preparation of the accounts for the financial year ended 31st March, 2006, the applicable accounting standards have been followed along with proper explanation relating to material departures;

(ii) that the Directors have selected such accounting policies and applied them consistently and made judgements and estimates that were reasonable and prudent so as to give a true and fair view of the state of affairs of the Company at the end of the financial year and of the profit of the Company for that period;

(iii) that the Directors have taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the provisions of the Companies Act, 1956 for safeguarding the assets of the Company and for preventing and detecting fraud and other irregularities; and

(iv) that the Directors have prepared the accounts for the financial year ended 31st March, 2006 on a 'going concern' basis.

LISTING OF BONDS ON LUXEMBOURG STOCK EXCHANGE

The Foreign Currency Convertible Bonds (FCCBs), due in 2018, aggregating to US$ 41 million issued on 15th April, 2005, pursuant to an option to subscribe for additional FCCBs under an International Offering of FCCBs of US$ 166 Million made in January 2005, were listed on the Luxembourg Stock Exchange. The FCCBs were converted into Global Depository Shares on 17th June, 2005.

SCHEMES OF ARRANGEMENT AND COMPROMISE

The Secured Redeemable Non Convertible Debentures of Rs.105/- each (debentures) held by holders of 2000 or less than 2000 fully paid debentures, holders of partly paid debentures and debenture interest holders have been restructured / settled in terms of the Schemes of Arrangement / Compromise sanctioned by the Hon'ble Gujarat High Court vide orders dated 7th October, 2004. Recently, the High Court by order dated 31st March, 2006 has sanctioned a Scheme of Arrangement and Compromise, with modifications, between the Company and Scheme Lenders comprising of the Rupee term lenders and the holders of more than 2000 debentures. As per the option exercised in terms of the scheme, the Company has paid the first installment of the debenture dues and the Scheme is fully implemented.

CORPORATE GOVERNANCE

In terms of clause 49 of Listing Agreement with the Indian Stock Exchanges, a certificate from Auditors of the Company on compliance of conditions of Corporate Governance is annexed to Directors' Report. A report on Corporate Governance as provided in clause 49 of the Listing Agreement is included in the Annual Report.

PARTICULARS OF EMPLOYEES

Information as per section 217(2A) of the Companies Act, 1956 read with the Companies (Particulars of Employees) Rules, 1975, as amended, is given in the Annexure forming part of this Report. However, as per the provisions of section 219(1)(b)(iv) of the said Act, the Report and Accounts are being sent to all shareholders of the Company excluding the statement of particulars of employees u/s 217(2A) of the said Act. Any shareholder interested in obtaining a copy of this statement may write to the Company Secretary, for the same, at the Registered Office of the Company.

ENERGY, TECHNOLOGY AND FOREIGN EXCHANGE

Information in accordance with Section 217(1)(e) of the Companies Act, 1956 read with the Companies (Disclosure of the Particulars in the Report

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of the Board of Directors) Rules, 1988 relating to the conservation of energy and technology absorption is not provided, as the same is not applicable to the Company. The Refinery Project is under implementation. Appropriate steps are being taken for the conservation of energy and effective absorption of technology.

Particulars relating to Foreign Exchange outgo and earnings appear in Note Nos. 6, 7 and 8 of Schedule XIX to the Annual Accounts.

FIXED DEPOSITS

Your Company has not accepted any deposits from public under section 58A of the Companies Act, 1956 during the financial year under report.

SUBSIDIARY COMPANY

As required under section 212 of the Companies Act, 1956, the audited statements of accounts along with the report of the Board of Directors and the Auditors' Report thereon of the subsidiary company, Vadinar Power Company Limited, for the financial year ended 31st March, 2006 are included in the Annual Report.

CONSOLIDATED FINANCIAL STATEMENTS

The Consolidated Financial Statements of the Company and its subsidiary, Vadinar Power Company Limited, prepared in accordance with Accounting Standard AS-21 on Consolidated Financial Statements form part of the Annual Report.

AUDITORS AND AUDITORS' REPORT

M/s. Deloitte Haskins & Sells, Chartered Accountants, Mumbai, Auditors of the Company hold office until the conclusion of the ensuing Annual General Meeting.

M/s. Deloitte Haskins & Sells, Chartered Accountants, Mumbai, have informed the Company that, if appointed, their appointment will be within the limits prescribed under section 224(1B) of the Companies Act, 1956. Accordingly, the members' approval is being sought to their appointment as the Auditors of the Company at the ensuing Annual General Meeting.

The observations of the Auditors in the Audit Report are explained wherever necessary in the appropriate notes to accounts and are self explanatory.

ACKNOWLEDGEMENT

The Board wishes to express appreciation and place on record its gratitude for the faith reposed in and co-operation extended to the Company by the Government of India, State Governments, various Government Agencies / Departments, Financial Institutions, Banks, Customers, Suppliers and Investors of the Company. Your Directors place on record their appreciation of the dedicated and sincere services rendered by the employees of the Company.

For and on behalf of the Board of Directors

Mumbai	**A N SINHA**	**P S RUIA**
28th August, 2006	Managing Director & CEO	Director

Annexures forming part of the Directors' Report

MANAGEMENT DISCUSSION AND ANALYSIS REPORT

Industry Outlook

It is now well known that energy prices have risen to unexpected and alarmingly high levels in the last three years. After rising from a price of US$ 23 per barrel in mid 2003 to US$ 52 per barrel in April 2005, the bench mark Brent crude prices hovered around US$ 62 per barrel in March 2006, representing an increase of 20% over a year and almost three times in three years. International prices are currently in the region of US$ 70 per barrel. Average prices of the Indian basket of crude has also gone up from US$ 39 per barrel in 2004-05 to US$ 55 per barrel in the current fiscal year. The reasons for these runaway price increases can be attributed to exceptionally robust economic growth, capacity constraints in the downstream refining sector, speculation by the trading community, geo political tensions and fear of natural calamities.

The Indian petroleum industry went through mixed fortunes as a result of the dynamics of price movements in international markets. The Government's compulsion to restrict price increases of petroleum, diesel, kerosene and LPG (domestic) at the retail level meant that its Oil Marketing companies suffered huge losses on retail sales, partly compensated through oil bonds. Oil refining companies however, saw Gross Refining Margin (GRM) remaining healthy between US$ 5.50 to US$ 10 per barrel depending on the technological capability and end product mix of the refinery. Your Company, a pure marketing company, suffered as it had to purchase products at international prices and retail them at artificially low prices determined by the Government.

Refinery capacities in India are expected to go up to 184 million tonnes per annum by 2011–12 from the current levels of 132 million tonnes, but with the rapid growth in the economy, specially the automobile sector, demand for motor spirit and high speed diesel is expected to show similar growth trends. This coupled with huge international demand for petroleum products, augers well for the companies in the refining sector.

The Auto fuel policy of the Government of India and the international trend to move towards cleaner fuels with lower sulphur and benzene content mean that refineries with the capability to produce EURO II, III & IV in terms of premium pricing and demand. Your Board of Directors believes that the Company's refinery is coming up at an opportune time and its further technological up-gradation and re-configuration to produce higher grade and higher quality fuels will be of considerable advantage.

Marketing

The demand for motor spirit and high-speed diesel remained strong with the auto sector riding high on the back of a robust economic growth. However, the Government's reluctance to allow increase in retail prices in line with rising crude oil and product prices, led to a very piquant situation for your Company. The more we sold, the more we lost.

In this unenviable situation, your Company has taken the following approach to marketing its product:

- We are not pursuing bulk sales to industrial consumers other than State Transport undertakings where we have firm supply contracts.
- Your Company is faced with an extremely challenging situation in relation to expansion of its retail outlets. However, as a long-term strategy and in the hope that this anomaly in pricing has to find a correction in the near future, your Company has strengthened its retail network to 700 (as on March 31, 2006) from 500 last year. Your Company appreciates the hardship faced by the franchisees who have had to contend with lower supplies and has structured a suitable compensation package for them.

We believe that our business model is designed to create a win-win situation for the consumer, the franchisee and the company. We operate on the principle of quality, optimum cost and reasonable operating returns and in

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the current adverse context, the low cost franchisee based model we have chosen for our retail business is considered the most appropriate.

The Refinery

Your Directors are pleased to report that the refinery project is proceeding at a rapid pace. It may be recalled that as per the terms of agreement with the Financial Institutions, the commissioning of the refinery is to be completed in April 2007. Your Company has set a target of commissioning the first phase of the refinery six months in advance. All necessary infrastructure such as power, oil terminal facilities for receipt of crude and dispatch of products, tankages etc. are at final stages of completion. Primary process units are at the pre–commissioning stage.

A significant development in the re-start of the project has been the Company's ability to modify the configuration to produce middle distillates, the largest and fastest growing segments of the domestic and international markets. This will ensure that we are at the upper end of the "Gross Refinery Margin" chain when we complete the commissioning of the refinery.

Our pre-commissioning, commissioning, operation and maintenance task forces are already in place and we are hopeful of a successful hand over from the project teams.

We have completed the first phase of the township for our refinery staff and they are now able to live close to the refinery.

Quality Assurance

Your Company is in the process of setting up a modern laboratory spread over an area of 1600 square meters. It will be equipped with modern, state-of-the-art instrumentation such as UV spectrophotometers, Octane / Cetane engines, JFTOT, CFPP, etc. The laboratory will be staffed by a highly skilled and experienced team and will provide 24x7 support to the operating units and blending teams, random testing of market samples and certification. The laboratory will also be responsible for advising the refinery on parameters related to environmental matters and other regulatory issues.

International Supply and Trading

An international supply and trading group has been set up at Mumbai, to manage the supply, scheduling, optimised operations and trading of crude as well as finished products. A core team of experienced industry professionals has been recruited. Intensive class room and 'on-desk' training programmes are being conducted for personnel who will manage this function. Your Company has also installed a contemporary software system to assist in the selection of optimum crude oils and product slate and also manage price risks associated with the refinery business.

Upstream Activities

The high crude oil prices and increasing demand have resulted in a positive market sentiment in the Exploration & Production business. However, intense competition in the upstream oil and gas industry has also led to increased costs across all areas of manning, equipment and exploration services. Several public and private sector companies and international companies are actively pursuing opportunities in this sector as the Government continues to encourage exploration activity.

Your Company has drilled three oil and gas wells and two appraisal wells in the Cambay basin (CBON3) to evaluate the discovery of oil and is in the process of formalising a development plan.

Your Company expects to receive the final approval of the Production Sharing Contract (PSC) shortly from the Government of India for the "Ratna and R Series Fields" which has in-place reserves of approximately 500 million barrels. Your Company has a 50% share in these fields with ONGC having 40% and Premier Oil 10%.

There has been a delay in the Company's Assam block due to non-availability of deep drilling rig. The Company plans to commence drilling in this block towards the end of the year. The Company has sought permission from the Government for exploitation of Coal Bed Methane (CBM) gas from the Raniganj block in West Bengal.

During the year, your Company signed one on shore and one offshore exploration and development block agreement with the Government of Myanmar and this is currently in the exploration phase. Your Company has a 25% participating interest in each of these blocks and considers these agreements as significant development in the business plan of the E & P division.

Planning for the future

The Business Development Group of your Company is in the midst of preparing a long term plan to further increase refinery capacity to 14 MMTPA initially and enhance it to 32 MMTPA in the second stage and equip itself with the capability to produce products across the value chain that most modern petroleum and petrochemical complexes the world over strive to achieve. The up-gradation and optimization will involve additional investments in process units and secondary facilities, the planning for which is already under way.

Financial Highlights

Your Company earned total income of Rs. 699.22 crore in the twelve months ended 31st March, 2006 as against Rs. 1146.58 crore in the fifteen months ended 31st March, 2005. The under– recoveries in the marketing of transport fuels on account of Government policy forced the Company to drastically curtail its sales during the year, resulting in the steep decline in total income. The loss after tax of Rs. 93.68 crore during the year under review was also for the same reason and was considered necessary to establish and maintain marketing infrastructure within domestic market until such time the refinery is fully commissioned and the Government allows oil marketing companies to adjust retail prices of fuels to match international price movements of crude.

Human Resources

Your Company strives to create a Human Resource team that is committed to participating in the growth and development of the organisation, while deriving job enrichment and satisfaction for themselves. The employee strength as of July 31, 2006, is over 1300 which is more than double the number employed at the same time last year. The Company concentrated on hiring talent from various engineering and management institutes, as well as induction of experienced professionals from related industries.

Your Company has developed a structured system for identifying training and developmental needs of the organisation and has created learning forums to foster collective learning and team work. The Company has set up an in-house training centre called the Essar Learning Centre to impart training in Knowledge and skills.

Internal Controls

Your Company had undertaken the implementation of SAP R3 software, which is an Enterprise Resource Planning (ERP) package. The system went "live" on April 1, 2006. The Company has initially implemented FI / CO (Finance & Control), MM (Materials Management) and SD (Sales & Distribution) modules and plans to implement additional modules during the current year.

Your Company continues to ensure that all material transactions are recorded properly and adequate protection exists against significant misuse or loss of Company assets. With the increased activities at the refinery project site, your Company has also strengthened the internal audit department to cope with the additional requirements. The utilization of funds for the Refinery project continues to be monitored by an independent and reputed accounting firm and by an international engineering firm on behalf of the lenders.

Safety, Health and Environment

Your Company has set up a Health, Safety, Environment and Fire Services department to ensure compliance with all statutory requirements and also to ensure safe start-up, commissioning and regular operations of the Refinery. Occupational health and emergency medical treatment facilities

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have already been set up, emergency vehicles such as fire fighting vehicles and ambulances etc. have been procured and made available at the site.

Your Company has obtained all necessary environmental clearances. Your Company has been regularly sending compliance reports of these clearances to the concerned authorities.

As a measure of environmental protection, your Company has installed a state-of-the-art waste water treatment plant for treating refinery waste water. It has also installed a desalination plant to produce sweet water from sea water.

To ensure that air emission from the refinery does not have an adverse effect on the surrounding area, your Company plans to install flue gas desulphurization units in the power plant as well as the Fluid Catalytic Converter Unit (FCCU).

Your Company has planned for creating a green belt in an area of over 1000 acres at the refinery site, out of which 416 acres have already been developed.

Your Company is seized of its responsibility for protection of the ecology, especially as it operates in a highly eco-sensitive area like the Gulf of Kutch. It has taken adequate precautions in terms of equipment and systems to preserve the marine life in the region.

Social Responsibility

In keeping with its philosophy of concentrating on social responsibility programs that are relevant and useful to the communities in and around its manufacturing facilities, your Company continued activities aimed at improving their environment and life style. Besides supporting local schools and hospitals, we organise blood donation drives, equip community centres with medical equipment and conduct regular health camps for villages in the vicinity. Our major contribution has been in the form of direct and indirect employment to the youth in the vicinity and creation of self employment opportunities.

Cautionary Statement

Certain words and statements in this Management Discussion and Analysis are forward looking statements based on numerous assumptions regarding your Company's present and future business strategies and the environment in which your Company will operate in the future. The important factors that could cause actual results, performance or achievements to differ materially from such forward-looking statements include, among others, changes in demand and supply, government policies or regulations, political and economic development within and outside India and, in particular, changes relating to the administration of oil and gas industry.

For and on behalf of the Board of Directors

Mumbai	**A N SINHA**	**P S RUIA**
28th August, 2006	Managing Director & CEO	Director

AUDITORS' CERTIFICATE

To

The Members of Essar Oil Limited

We have examined the compliance of conditions of Corporate Governance by Essar Oil Limited ("the Company"), for the year ended 31st March, 2006 as stipulated in clause 49 of the Listing Agreement entered into by the said company with stock exchanges in India.

The compliance of conditions of Corporate Governance is the responsibility of the Management. Our examination was limited to procedures and implementation thereof, adopted by the Company for ensuring the compliance of the conditions of the Corporate Governance. It is neither an audit nor an expression of opinion on the financial statements of the Company.

In our opinion and to the best of our information and according to the explanations given to us, we certify that the Company has complied in all material respects with the conditions of Corporate Governance as stipulated in the above-mentioned Listing Agreement.

We further state that such compliance is neither an assurance as to the future viability of the Company nor the efficiency or effectiveness with which the Management has conducted the affairs of the Company.

For **Deloitte Haskins & Sells**
Chartered Accountants

N P Sarda
Partner
Membership No. 9544
Mumbai, 28th August, 2006

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