ESSAR

# Essar Oil Limited

## Annual Report 2006 - 2007

## BOARD OF DIRECTORS (As on 30th August, 2007)

| | |
|---|---|
| Shashi Ruia | *Chairman* |
| Ravi Ruia | *Vice Chairman* |
| Prashant Ruia | |
| Anshuman Ruia | |
| Awadhesh N. Sinha | |
| 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.* |
| V. K. Sinha | *Nominee of LIC of India* |

## COMPANY SECRETARY

Sheikh S Shaffi

## BANKERS

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



## AUDITORS

M/s. Deloitte Haskins & Sells, Mumbai

## REGISTERED OFFICE

Khambhalia Post, Post Box No. 24
Dist.: Jamnagar - 361 305, Gujarat
Tel.: 02833 - 241444
Fax: 02833-241616 /241414
E-mail : eolinvestors@essar.com

## 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<br>Dalal Street, Mumbai - 400 023 |
| National Stock Exchange of India Ltd. | Exchange Plaza, 5th Floor, Plot No. C/1<br>G Block, Bandra-Kurla Complex<br>Bandra (E), Mumbai - 400 051 |

# NOTICE

NOTICE is hereby given that the **Seventeenth 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 Saturday, the **29th September, 2007** at **11:30 a.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, 2007, 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 Ravikant N Ruia who retires from office by rotation and being eligible, offers himself for reappointment.
3. To appoint a Director in place of Shri Awadhesh N Sinha 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 a Special Resolution:

   "RESOLVED THAT in accordance with the provisions of sections 81, 81(1A) and other applicable provisions, if any, of the Companies Act, 1956 and enabling provisions of the Memorandum and Articles of Association of the Company, the Listing Agreements entered into by the Company with the Stock Exchanges, where the shares of the Company are listed and in accordance with the guidelines issued by the Government of India (GOI), the Reserve Bank of India (RBI), the Securities and Exchange Board of India (SEBI) and / or any other competent authorities and clarifications thereof, issued from time to time, and subject to such approvals, permissions, consents and sanctions as may be necessary from the GOI, RBI, SEBI and/or any other competent authorities and subject to such conditions and modifications as may be prescribed or imposed by any of them while granting such approvals, permissions, consents and sanctions, which may be agreed to by the Board of Directors of the Company (hereinafter referred to as "the Board" which term shall include any committee constituted / to be constituted by the Board for exercising the powers conferred on the Board by this resolution), the consent of the Company be and is hereby accorded to the Board to create, offer, issue and allot, in one or more tranches, outside India, with or without premium, denominated in any foreign currency, such number of optionally/ compulsorily convertible/redeemable Foreign Currency Convertible Bonds (FCCBs) and / or Global Depository Receipts (GDRs) and / or American Depository Receipts (ADRs) and / or Fully / Partially Convertible Bonds / Loans and / or any other instruments / securities in the nature of Shares and / or warrants, naked or otherwise, convertible into Shares or otherwise, either in registered or bearer forms, and / or any such security convertible into equity shares with face value of Rs.10/- each or otherwise (hereinafter referred to as 'financial instruments') or any combination of the financial instruments in the International Market, aggregating to an amount not exceeding USD750,000,000/- (United States Dollars seven hundred fifty million only) to Essar Energy Holdings Limited (formerly Prime Finance Company Limited), Mauritius, the existing Promoters and/or its associates / nominees / group companies/ persons acting in concert, whether or not they are members of the Company, on preferential issue basis, to the extent and in the manner as may be decided by the Board in this behalf."

   "RESOLVED FURTHER THAT :

   i. The equity shares issued upon conversion of financial instruments, so issued and allotted shall rank pari-passu with the existing equity shares of the Company;
   ii. For the purpose of giving effect to this resolution, the Board be and is hereby authorised to do all such acts, deeds, matters and things as the Board may, in its absolute discretion, consider necessary, proper, expedient, desirable or appropriate for making the said issue as aforesaid and to settle any question, query, doubt or difficulty that may arise in this regard including the power to allot under subscribed portion, if any, in such manner and to such persons(s) as the Board, may deem fit and proper in its absolute discretion to be most beneficial to the Company."

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

   "RESOLVED THAT pursuant to the provisions of Section 293(1)(a) and all other applicable provisions, if any, of the Companies Act, 1956 and in partial modification of the earlier resolutions passed at the Extraordinary General Meeting of the Company held on 4th October, 1994, the Ninth Annual General Meeting of the Company held on 2nd July, 1998 and at the Extraordinary General Meeting of the Company held on 17th September, 2003, consent of the Company be and is hereby accorded to the Board of Directors of the Company, including any committee thereof, for creating mortgages and/or charges, hypothecation, pledge and/or any other encumbrances on such terms and conditions and at such time(s) and in such form and manner as it may think fit, on all or any of the movable or immovable properties of the Company, wheresoever situated, both present and future or the whole or substantially the whole of any one or more of the Company's undertaking(s) in favour of all or any of the financial institutions, banks, lenders, financiers, trustees, investing agencies, bodies corporate, corporations, foreign institutional investors, any other person(s)/entities, or any combination of the above to secure rupee loans, foreign currency loans, debentures, bonds, convertible loans, fully/partly paid convertible / non-convertible bonds, any other securities / instruments, financial assistances or any other debt instruments (by private placement basis or otherwise) of an equivalent aggregate amount not exceeding Rs.25,000 Crore (Rupees twenty five thousand crore only) in Indian Rupees and / or in Foreign Currency together with interest thereon at the respective agreed rates, compound interest, additional interest, liquidated damages, commitment charges, premia on pre-payment or on redemption, Debenture/Security trustees remuneration, costs, charges, expenses and all other monies payable by the Company to the aforesaid parties or any of them under the agreements entered into / to be entered into by the Company in respect of the said loans, debentures, bonds, financial assistances and / or other instruments".

"RESOLVED FURTHER THAT the mortgages and / or charges, hypothecation, pledge and/or any other encumbrances to be created by the Company as aforesaid may rank pari passu with the mortgages and/or charges, hypothecation, pledge and/or any other encumbrances already created and/or to be created in future by the Company or in such other manner and ranking as may be thought expedient by the Board of Directors and as may be agreed to between the concerned parties."

"RESOLVED FURTHER THAT the Board of Directors of the Company be and is hereby authorised to finalise with any or all of the aforesaid parties, the documents, agreements, undertakings, bonds and writings for creating the mortgages / charges / hypothecation / pledge and/or any other encumbrances and accepting or making any alterations, changes, variations to or in the terms and conditions, and to do all such acts, deeds, matters and things and to execute all such documents, agreements, undertakings, bonds and writings as it may consider necessary, proper, desirable, appropriate or expedient for the purpose of giving effect to this resolution and to resolve any question, query, doubt or difficulty relating thereto or otherwise considered by the Board of Directors to be in the best interest of the Company."

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

   "RESOLVED THAT pursuant to the provisions of Section 293(1)(d) and other applicable provisions, if any, of the Companies Act, 1956 and Articles 96 and 99 of the Articles of Association of the Company and in partial modification of the earlier resolutions passed at the Extraordinary General Meetings of the Company held on 4th October, 1994 and 17th September, 2003, the Company hereby accords its consent to the Board of Directors for borrowing or continuing to borrow any sum or sums of money, from time to time, from any one or more of the Company's bankers and/or financial or investment institutions and/or from anyone or more other persons, firms, entities, bodies corporate, companies, whether by way of cash credit, advance or deposits, loans or bill discounting or otherwise and whether unsecured or secured, and if secured by mortgage, charge, hypothecation or lien or pledge or any other encumbrances of the Company's assets and properties whether movable or stock-in-trade (including raw materials, stores, spare parts and components in stock or in transit) including uncalled capital and work-in-progress and all or any of the undertakings of the Company notwithstanding that the moneys to be borrowed together with moneys already borrowed by the Company (apart from temporary loans obtained from the Company's bankers in the ordinary course of business) will or may exceed the aggregate of the paid-up capital of the Company and its free reserves, that is to say, reserves not set apart for any specific purpose but, so however, that the total amount upto which the moneys may be borrowed by the Board of Directors and outstanding at any time shall not exceed the sum of Rs. 25,000 Crore (Rupees Twenty Five Thousand Crore only) over and above the aggregate of the paid up share capital of the Company and its free reserves."

By Order of the Board of Directors

Mumbai
30th August, 2007

**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, i.e. before 11:30 a.m. of 27th September, 2007.**
2. The Register of Members and Share Transfer Books of the Company will remain closed from Friday, the 28th day of September, 2007 to Saturday, the 29th day of September, 2007 (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.

6. Directors retiring by rotation:

   **Shri Ravikant N Ruia**, Vice Chairman, belongs to the generation of industrialists who has played a significant role in strengthening India's industrial renaissance. An engineer by training, his entrepreneurial abilities have enabled the Essar Group to be one of the leading corporate houses of India, with a current asset base of over USD10 billion. The Group's interests span the core sector industries of Steel, Energy, Power, Communications, Shipping & Logistics and Construction. He is 58 years old.

   The other companies in which Shri R N Ruia is a Director are: Consolidated Fabrics Ltd., Copper Canyon Holdings Ltd., Energy II, Essar Global Ltd., Essar Infrastructure Holdings Ltd., Essar Investments Ltd., Essar Power Ltd., Essar Shipping Ltd., Essar Steel Ltd., Essar Steel Caribbean Ltd., Essar Steel Caribbean Holdings Ltd., Essar Steel (Hazira) Ltd., Essar Steel Sharjah FZE, Energy Transportation Ltd., Grand Pinnacle Investments Ltd., Grand Richmond Investments Ltd., Vodafone Essar Ltd., India Securities Ltd., International Fabrics Ltd., Primus Group Invest Ltd., Zeni Group Invest Ltd., Essar Minerals St. Lucia Ltd. He does not hold any shares in the Company. Shri R N Ruia retires by rotation at the Annual General Meeting and offers himself for reappointment.

   **Shri Awadhesh N Sinha** was the Managing Director & CEO of the Company for a period of three years from 31st January, 2004 to 30th January, 2007. Since then he is on the Board as Non Executive Director. He has done MSc and MBA in Marketing. He is 69 years old and has over 47 years experience in the oil and gas industry. In his career he has been associated with IOC for over 30 years where he headed various positions and rose to the level of Executive Director and a Board member of IOBL - a subsidiary of IOC. He has also served as Chief Executive (Marketing) with Essar Oil and President (Business Development) of Reliance Petroleum. Before joining Essar Oil as Managing Director & CEO he was with ONGC. The other companies in which Shri A N Sinha is a Director are: Essar Pipelines Ltd. and Petronet India Ltd. He is a member of Banking & Finance Committee, Investors' Relations Committee and Committee of Directors (Capital Issues) of the Board. He does not hold any shares in the Company. Shri A N Sinha, retires by rotation at the Annual General Meeting and offers himself for reappointment.

   **Shri Hari L Mundra,** Dy. Managing Director & Director (Finance) retires by rotation at the Annual General Meeting and does not offer 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**

The Company is implementing a 10.5 million metric tonne per annum Oil Refinery at Vadinar, District Jamnagar in State of Gujarat. Trial runs of certain units of the Refinery have commenced and the Refinery at full capacity ("Base Refinery") is expected to be commissioned shortly.

It is proposed to expand the refining capacity of the Refinery to 16 MMTPA. The expansion of refinery would enable the Company to process heavy and sour crudes while improving the product slate substantially. Simultaneously, the refinery is also being upgraded to meet the Euro III and Euro IV product specifications proposed to be implemented from 2010. The Gross Refining Margins of the refinery will improve significantly upon completion of the expansion and upgradation project. The proposed expansion project entails an expenditure of USD 1180 million, which is proposed to be funded through a mix of equity, internal accruals and debt.

In terms of approval received from the members at the 15th Annual General Meeting held on 30th September, 2005, USD 78 million have been brought in through issue of Global Depository Shares (GDSs). Now for funding the expansion of the Refinery, meeting any shortfall in funding / escalation in the cost of the expansion and for other general corporate requirements, infusion of additional equity of upto USD 750 million is envisaged.

Accordingly, the Company proposes to offer outside India such number of FCCBs and/or GDRs and/or ADRs and/or Convertible Bonds and/or any other financial instruments convertible into equity shares of face value of Rs.10/- each or otherwise in one or more tranches to Promoter Company viz; Essar Energy Holdings Limited and/or its associates/ nominees/Group companies/persons acting in concert on preferential issue/allotment basis for an amount not exceeding USD750 million (United States Dollars seven hundred fifty million only). In terms of The Foreign Exchange Management (Transfer or issue of security by a person resident outside India) Regulation, 2000 [FEM(TISPRO) Regulations], the Relevant Date for the determination of applicable price for the issue of equity shares upon conversion of any financial instruments is 30th August, 2007.

In terms of Section 81(1A) of the Companies Act, 1956, consent of the members is required by passing Special Resolution in General Meeting for allotment of further equity shares to any person other than the existing share holders.

At the time of conversion of convertible securities into equity shares, the Company will ensure compliance with conditions of continuous listing of the listing agreement entered into with Stock Exchanges.

Consent of the members is therefore sought to authorise the Board of Directors to create, offer, issue and allot FCCBs and/or ADRs and/or GDRs and/or other convertible financial instruments and upon conversion, issue and allot equity shares, in the manner setout in Item No. 5 of the Notice.

The Directors accordingly recommend the resolution at Item no. 5 for your approval.

Shri S N Ruia, Shri R N Ruia, Shri P S Ruia and Shri A S Ruia, Directors of the Company, may be treated as concerned or interested in the resolution 5. None of the other Directors is concerned or interested in the resolution.

**Item Nos. 6 and 7**

Presently, the Board of Directors can borrow an amount not exceeding Rs.20,000 crore over and above the paid up capital and free reserves and create security in the form of mortgages and/or charges, hypothecation, pledge or any other encumbrances on the assets of the Company upto Rs.20,000 Crs.

The amount already borrowed and the funds to be borrowed in future, is expected to exceed the above limit. To meet the various operational requirements of the Company including part financing cost of the expansion and upgradation of the Refinery, meeting various working capital requirements and Marketing and Exploration & Production activities, it is necessary to increase the limit up to Rs.25,000 crore.

In terms of Section 293(1)(a) of the Companies Act, 1956, the members' approval is required to create mortgages and/ or charges, hypothecation, pledge or any other encumbrances on the assets of the Company. The resolution setout at item no. 6 of the Notice will enable the Company to create mortgage in favour of one or more of the lenders and / or financiers and / or trustees to the issue of secured debt instruments in respect of borrowings for an amount not exceeding Rs.25,000 Crore. Further, section 293(1)(d) of the Companies Act, 1956 stipulates that approval of the members is required for borrowings in excess of paid-up share capital and free reserves of the Company.

The Directors accordingly recommend the resolutions at item nos. 6 and 7 for your approval.

None of the Directors of the Company is in any way concerned or interested in the resolutions.

By Order of the Board of Directors

Mumbai
30th August, 2007

**SHEIKH S. SHAFFI**
Company Secretary

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

# DIRECTORS' REPORT

**To the Members of Essar Oil Limited**

Your Directors have pleasure in presenting the Seventeenth Annual Report together with the audited accounts of the Company for the financial year ended March 31, 2007.

**FINANCIAL RESULTS**

(Rs. in crore)

| | 2006-2007 | 2005-2006 |
|---|---|---|
| Gross Income | 484.37 | 699.22 |
| Gross Profit / (Loss) | (50.04) | (87.39) |
| Less: Depreciation | 4.51 | 4.66 |
| Profit / (Loss) before Income Tax | (54.55) | (92.05) |
| Less: Provision for Income Tax /Foreign Tax / Deferred Tax Liability / Fringe Benefit Tax | 12.94 | 1.63 |
| Net Profit / (Loss) | (67.49) | (93.68) |
| Add: Balance brought forward from previous year | 7.71 | 82.89 |
| Add: Transfer from Foreign Project Reserve | 39.51 | 18.50 |
| Total amount available for appropriations | (20.27) | 7.71 |
| Less: Appropriations | | |
| (a) Foreign Projects Reserve | — | — |
| (b) Debenture Redemption Reserve | — | — |
| (c) Transfer to General Reserve | — | — |
| (d) Proposed Dividend | — | — |
| Balance to be carried to Balance Sheet | (20.27) | 7.71 |

**INCREASE IN THE SHARE CAPITAL**

During the year, the paid up capital of the Company increased from 108,35,77,314 equity shares of Rs.10/- each to 113,95,30,638 equity shares of Rs.10/- each upon issue of 5,59,53,324 equity shares of Rs.10/- each to the overseas depository for Global Depository Shares (GDSs) on allotment of GDSs aggregating to USD78 million to Promoters on preferential issue basis pursuant to approval granted by the shareholders at the 15th Annual General Meeting held on 30th September, 2005. The issue proceeds have been utilised for the implementation of the Refinery Project.

**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 setout as Annexure B to the Directors' Report and has been prepared in compliance with the terms of clause 49 of the Listing Agreement with Stock Exchanges.

**DIRECTORS**

Shri Awadesh N. Sinha was functioning as Managing Director and CEO upto 30th January, 2007 and thereafter he is continuing as Non Executive Director on the Board. During the year Shri V. K. Sinha was appointed as Nominee Director of Life Insurance Corporation of India.

Shri Ravikant N Ruia and Shri A. N. Sinha retire by rotation at the ensuing Annual General Meeting and offer themselves for re-appointment. Shri Hari L. Mundra retires at the Annual General Meeting and does not offer himself for reappointment.

**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, 2007, 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, 2007 on a 'going concern' basis.

**CORPORATE GOVERNANCE**

In terms of clause 49 of Listing Agreement with the Stock Exchanges, a certificate from Auditors of the Company on compliance of conditions of Corporate Governance is annexed to the Directors' Report as Annexure C. 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**

The particulars as prescribed under section 217(2)(e) of the Act read with the Companies (Disclosures of Particulars in the Report of Board of Directors) Rules, 1988 are setout in Annexure A to this Report.

Particulars relating to Foreign Exchange outgo and earnings appear in Note No. B(11) of Schedule XVII 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, 2007 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

| | | |
|---|---|---|
| | **HARI L MUNDRA** | **P S RUIA** |
| Mumbai | Dy. Managing Director & | Director |
| 30th August, 2007 | Director (Finance) | |

## Annexure A to the Directors' Report

**STATEMENT OF PARTICULARS UNDER THE COMPANIES (DISCLOSURE OF PARTICULARS IN THE REPORT OF BOARD OF DIRECTORS) RULES, 1988**

**A. CONSERVATION OF ENERGY**

a) **Energy Conservation measures taken: -**

Your Company maintains its thrust on fuel conservation right from the design and commissioning stage. Including commissioning fuel, total fuel & loss during the year was 4.95%, which is an achievement. State of the art technology has been adapted for accurate measurement e.g. Radar-gauges for crude oil & heavy product storage tanks and mass flow meters for product dispatches. Dedicated energy group has been set-up at the refinery for close monitoring and improvement of energy performance. Energy conservation measures are under constant focus of the management and all efforts are being made to become a pace-setter refinery through continuous improvement.

Energy conservation features have been incorporated in the design of plant itself. Some of the important features of the Refinery are:

- Low level heat recovery (Crude column overhead Vs. Crude)
- Use of compressors for crude column overhead gases & operation of crude column at low pressure.
- Use of low pressure steam for Vacuum column Ejectors.
- Use of Vacuum Hydro-circulating system in the Dryer of DHDS.

b) **Additional Investments and Proposals, if any, being implemented for energy conservation:**

Certain units of refinery have been commissioned recently. Energy conservation efforts are given high priority. Elaborate energy accounting system is in place which is reviewed periodically. Once all the facilities are commissioned, energy conservation study for bench-marking in the performance will be undertaken by a reputed international agency.

c) **Impact of the measures at (a) and (b) above for reduction of energy consumption and consequent Impact on the cost of production of goods:**

Impact will be assessed once the refinery is operated at full throughput with associated secondary processing facilities.

d) **Total energy consumption and energy consumption per unit of production as per Form 'A' is attached hereto:**

**B. TECHNOLOGY ABSORPTION**

The Refinery has adapted the following technologies for deriving the latest technological advances:

| | | |
|---|---|---|
| Crude/Vacuum Distillation Unit | : | ABB Lummus Crest, Netherlands |
| Visbreaker Unit | : | Axens, France |
| Catalytic Reforming Unit | : | Axens, France |
| Diesel Hydro-desulphurization Unit | : | Axens, France |
| Fluidized Catalytic Cracking Unit | : | Stone & Webstar, USA |

**FORM A**

| | | 2006-2007 * |
|---|---|---|
| **A)** | **Power and Fuel Consumption:** | |
| **1** | **Electricity** | |
| | **(a) Purchased** | |
| | Unit ('000 KWH) | 27,122.00 |
| | Rate /Unit | 6.99 |
| | Total Amount ( Rs in Lakh) | 1,896.00 |
| | **(b) Own Generation** | |
| | (i) Through Diesel Generator | N.A. |
| | Unit ( '000 KWH) | |
| | KWH per litre of diesel oil | |
| | Cost / Unit ( Rs./KWH) | |
| | (ii) Through Steam Turbine/Generator | |
| | Unit ( '000 KWH) | 72,326.00 |
| | KWH per litre of Fuel Oil/ Gas | 1.24 |
| | Cost / Unit ( Rs./KWH) | 4.86 |
| | **(c) Electricity Consumed** | |
| | ( a+b) (' 000 KWH) | 99,448.00 |
| **2** | **Coal (specify quality and where used)** | N.A. |
| **3** | **Furnace Oil/ other Liq fuels-Purchased** | |
| | Quantity ( MT) | 16,665.00 |
| | Amount ( Rs. In Lakhs) | 2,947.23 |
| | Average Rate ( Rs./MT) | 17,685.15 |
| **4** | **Others/From Internal Generation Fuel** | |
| | **(i) Fuel Gas** | |
| | Unit ( MTs) | 7,782.16 |
| | Amount ( Rs. In Lakhs) | 1,285.85 |
| | Average Rate ( Rs./MT) | 16,523.00 |
| | **(ii) Liquid Fuel-FO** | |
| | Unit ( MTs) | 64,065.70 |
| | Amount ( Rs. In Lakhs) | 8,789.81 |
| | Average Rate ( Rs./MT) | 13,720.00 |
| **5** | **Total Liquid Fuel - Purchased+Own Generation (MT)** | 80,730.70 |

| B | Consumption Per Unit of Production: | Unit | 2006-2007 * |
|---|---|---|---|
| | (i) Actual Production (MTs)- | | 1,662,500.00 |
| | (ii) Consumption per MT of Production | | |
| | - Electricity (Purchased+Generated) | KWH/MT | 59.82 |
| | - Liquid Fuel (FO/LSHS/NAPHTHA) (Purchased + Internal Generation) | MT/MT | 0.05 |
| | - Fuel Gas | MT/MT | 0.00 |

* Note : Certain units of Refinery commissioned trial production during the year starting from November, 2006 and hence there are no corresponding figures for the previous financial year 2005-2006.

**FORM B**

**TECHNOLOGY ABSORPTION**

The Company is making investment in Research and Development and planning to carryout the following activities in coming year:

**Future plan of action**

- Studies on fuel oil blending properties evaluation for various cutter stock combinations.
- To establish new laboratory facilities/equipment for Visbreaker vacuum residue and Fuel oil stability testing
- To set up TBP testing apparatus for characterization of various crudes/ Crude blends in the Laboratory
- New product development like Carbon Black Feed Stocks, Rubber Processing Oils, etc.

**Expenditure on R & D**

| | | | |
|---|---|---|---|
| A. | Capital | : | Rs. 525 Lacs |
| B. | Recurring | : | Rs. 50 Lacs |
| C. | Total | : | Rs. 575 Lacs |
| D. | Total expenditure as percentage of total turnover | : | Negligible |

## Annexure B to the Directors' Report

# MANAGEMENT DISCUSSION AND ANALYSIS

**Industry Outlook**

As the global demand for energy continues to grow, oil is expected to remain the main determinant of world economic growth in the foreseeable future. OPEC has indicated that based on a global economic growth rate of 3.5% per annum (purchasing power parity basis), the demand for oil is set to rise to 118 million barrels per day by 2030 from the current level of 85 million barrels per day.

The transportation sector is expected to be the main demand driver as more and more developing countries are expected to grow in terms of commercial vehicle and passenger car volumes. The non transportation sector will also grow, mainly in the developing nations of Asia and Africa, as petrochemical industry takes stronger roots there.

Based on the projections of demand for petroleum products, the total investment in refinery processing by the year 2020 is estimated to be around USD 450 billion including the cost of capacity expansion, new projects and ongoing maintenance and replacement. The Asia Pacific region will require the highest level of investments with China accounting for a major portion.

Environmental regulations will also play a critical role in terms of technology as well as product quality specifications of end products. The search for alternative fuels, though gathering pace and usage is not expected to have a significant impact on the demand for oil and its end products.

Almost the entire reserves in the world of "easy oil" have already been found and are being exploited. Those which are now increasingly being made available are "difficult oil" – difficult in geographical reach stretching logistics and sour, heavy and acidic which are difficult to refine and more difficult to manage environmentally.

The opportunity for your Company to increase refining capacity based on the above scenario is exciting. The need for ultra clean transport fuels to meet stringent environmental specifications for petroleum products is an opportunity that new refineries based on contemporary technology can take advantage of. These technologies offer not only product quality and specifications to the most stringent standards, but are also able to deal with heavier or highly sour crude. This enables maximum utilisation of crude input and allows for production of the most stringent end products translating into higher margins.

**The Indian Scenario**

The consumption of petroleum products in India during the year under review stood at 119.85 million metric tonnes (MMT), an increase of 5.9 % as compared to the previous year, contributed by growth in demand for transport fuels.

However, many refineries, especially those in the private sector are exporting petroleum products as global demand continues to be robust. Against domestic refining capacity of close to 150 MMTPA and consumption of around 120 MMTPA, the country continues to have surplus refining capacity. With several refineries planning capacity expansion, the surplus is expected to continue. Exports of petroleum products have reached a level of 32.4 MMT during the year under review. There are some strong reasons for private refineries in India looking outside their domestic markets and exporting a fair proportion of their products to protect their margins. Although international prices have being rising, domestic prices were not allowed to be increased and this has had a substantial adverse impact on the profitability of the oil marketing companies during 2006-07, given the fact that domestic production of crude oil was only 31.5 MMT against imports of 111 MMT during this year.

The sharp increases and more critically the wide fluctuations in crude oil prices in the last two years have made it virtually impossible for oil marketing companies to sustain margins. In spite of severe constraints in feeding their retail outlets with products, the private marketing organisations added over 700 outlets last year. Despite all efforts to convince Government to bring about a level playing field, these companies do not receive the kind of Governmental support that Public sector companies get in the form of Oil Bonds. The private sector oil marketing companies had made aggressive marketing efforts and in the last two years had gained a market share of close to 12% in a market dominated by the public sector. The Government's discriminatory approach in favour of public sector oil companies (by subsidising retail prices) has now resulted in the market shares of the private oil marketing companies dwindling to a mere 2%.

The Rangarajan Committee, constituted by the Government to look into various aspects of pricing and taxation of petroleum products, submitted its report in February 2006. The Committee has given recommendations relating to the pricing of MS, HSD, domestic LPG and SKO for supply through the Public Distribution System. Besides, it has also recommended restructuring of excise duties to make it a pure specific levy, instead of the current Ad valorem. Some of these recommendations have already been implemented, including the change in the basis of pricing of petrol and diesel from import parity to trade parity and reduction in customs duty from 10% to 7.5% on these products. This has, however, failed to make any significant impact on the under recoveries in the domestic marketing of transportation fuels.

**Marketing**

**Retail sales**

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 the anomaly in pricing has to find a correction in the near future, your Company has strengthened its retail network to 1178 (as on March 31, 2007) from 700 last year. Your Company has managed to reduce the impact of anomaly in pricing by higher prices in certain markets to contain demand coupled with a suitable compensation package for fanchisees to compensate lower thruput through their outlets. We operate on the principle of quality, optimum cost and reasonable operating returns and in the current adverse context, the low cost franchisee based model we have chosen for our retail business is considered the most appropriate.

The emphasis during the year was on selective network expansion and standardization. Your Company commissioned 513 new retail outlets, representing 16% of the 3200 new retail outlets commissioned by the industry during 2006-2007.

**Direct sales**

The year 2006-2007 has been a year of diversification for the Direct Sales business as, for the first time, the Company commenced marketing of Furnace Oil, from the refinery in the domestic market. The Company also commenced sale of LPG to PSUs from the refinery. It is pertinent to note that your Company is not allowed to sell these products directly since they are subsidised and can be sold only to the public sector companies.

A number of new initiatives were undertaken during the year in the area of customer service and technical support. These initiatives are expected to help retain the existing customers and facilitate tying up of new business. Intense competition and aggressive marketing by the Public Sector and private marketers will, however, continue to be the order of the day.

Your Company is seeking a level playing field between the PSUs and the private sector and has made representations to the Government for further liberalization and deregulation of the industry and restoration of a market determined pricing mechanism. This will enable the industry to invest in world class refining, retailing and exploration facilities and ensure the integration of India with the global Hydrocarbon industry. In this endeavour, we are one with other oil companies in the private sector like Reliance Industries Limited and Shell.

**The Refinery**

Your Directors are proud to report that 2006-2007 will be remembered as the landmark year in which the primary units of the refinery commenced trial operations along with various utilities and offsite facilities. This was achieved in November 2006 when crude was introduced into the crude and vacuum distillation units, the refinery's primary process facility. This was followed by the trial start-up of the Vis-breaker in January and the Continuous Catalytic Reformer and the Naphtha Hydro Treator in February.

Construction of the balance units of the Refinery is at an advanced stage. The major challenge facing the project team was in securing timely delivery of materials and equipment as a consequence of very strong world-wide construction activity which has resulted in delay in commissioning of the balance units. We expect the balance units to be commissioned in the next quarter.

In response to changes in current and forecasted product demand patterns, the refinery's processing capability has been adjusted to maximize production of middle distillates (Aviation Turbine Fuel and diesel). This change will ensure that the refinery will be positioned at the upper end of the "gross refinery margin" range when full operation is achieved.

To further optimize performance, the creation of additional treating capability, storage facilities and coastal despatch facilities are being expedited and construction is well underway. Construction of the GAIL pipeline for LPG from our Refinery to their existing Jamnagar-line System is also well underway providing us this most cost effective transportation mode to the high growth demand centres in North India.

During the trial run till 31st March, 2007 the Refinery produced 1.32 million metric tonnes of finished petroleum products. The expenses relating to trial runs are being capitalised pending completion of the Project.

**Quality Assurance**

Your company has a state-of-the-art laboratory which is well-equipped to monitor the quality of intermediate streams and certify the quality of final products before dispatch. It tests all samples from the consumer end to provide quality assurance. This Lab is well on its way to getting ISO accredition.

The laboratory is staffed by a highly skilled and experienced team that provides round the clock support to operations. It has been inspected and certified by DGCA (Director General of Civil Aviation).

As of 31st March, 2007, the laboratory had certified, without a single error over a Million tonnes of shipped product and over 10,000 road tanker loads of product.

**International Supply and Trading**

Oil prices were strong in the last year due to a number of reasons like robust world economic growth, supply disruptions, and geopolitical tensions. Dated Brent was stronger by over USD 6 per barrel over the last year averaging about USD 64.14 per barrel. Global oil demand growth however slowed slightly to 0.8 mbpd in 2006 from 1.2 mbpd in 2005. The premium for light products over fuel oils remained high, favouring complex refineries over less complex sites. Product quality continued to tighten worldwide; this is one of the last stages to virtual elimination of sulphur from transportation fuels.

Crude price movement of the past year can be divided into two distinct time periods viz. July to January and February onwards. In the first period, prices reached an all time high of USD 78.64 in July followed by a move to a low of USD 50.75 in January. For the past three years, oil prices have regularly dropped in this period by significant amounts. In the second period, prices retraced to its highs.

The first crude oil cargo for your company arrived at our SBM on 6th September, 2006. During the financial year, the Company contracted 26 mbls of crude oil on spot basis. Most of these grades were contracted from the West African and Mediterranean region. The Company exported 8 mbls of product valued around USD 517 million from the trial runs of some of the units. Our export markets are mainly in Far East Asia, Europe, Africa, Middle East and the US Gulf Coast. Your Company has also commenced risk management activity and are judiciously hedging crude imports, product exports and foreign exchange.

With the commissioning of the FCCU and DHDS during 2007-2008, our crude diet and product specifications will change substantially. The Company will be able to process sour, heavy and acidic grades and will explore the possibilities of terming up crude contracts through an optimum mixture of spot and term cargoes. The Company is already exploring new export markets for product evacuation. The aim will be to term up an optimum percentage of our product cargoes to mitigate off take risks. With the inclusion of more VLCC shipments and Middle Eastern crudes our freight bills are also expected to reduce considerably.

The combination of rising consumption, the continued effects of production cuts by members of the OPEC, and only modest increases in non-OPEC production is expected to pull the inventories down. Consequently, the prices are expected to remain strong. World oil consumption is projected to grow by 1.3 million bbl/d. But, slowdown in economic growth in the US may contribute towards weakening of oil prices.

**Upstream Activities**

Upstream oil and gas sector continues to be buoyed by high international crude oil and gas prices driven by astronomical growth in the emerging economies. Accordingly, market sentiment continues to be very positive for the Exploration & Production business worldwide. However, intense competition for resources has led to increased costs across all areas of manning, equipment and exploration and development services.

In the Indian context, several public and private sector companies and international companies are actively pursuing opportunities in oil and gas, as the Government continues to encourage investment in exploration activity. The Government conducted bidding rounds NELP-VI and CBM-III successfully, for award of acreage for exploration. NELP-VII is expected to be announced around September 2007.

Your Company has 11% participating interests in Mehsana (Gujarat) block. Commercial production has just commenced and further exploration activity in the same block continues in Phase II.

A Consortium comprising your Company (with 10% Participating Interest) and other parties was awarded two new blocks in the Assam (Arakan basin) under NELP-VI round of bidding.

Your Company expects to receive the long awaited final approval for the Production Sharing Contract (PSC) shortly for the “Ratna and R Series Fields” from the Government of India, in which the Company has a 50% share with ONGC having 40% and Premier Oil 10%.

Premier Oil, the field Operator in our existing exploration Block in Cachar District, Assam is currently drilling an exploratory well (Masimpur-3) where your Company has a 16% “carried interest”.

The Company has almost completed a program of drilling 12 core-wells in CBM Block, Raniganj East in West Bengal, where it has 10% participating interest. This has resulted in delineation of an area of about 100 sq. kms. where existence of adequate gas resources has been established. Your Company will next undertake test drilling in this area to establish commercial reserves.

Your Company has a 25% “carried” participating interest in one onshore and one offshore exploration block in Myanmar, operated by Essar Exploration & Production South East Asia Limited (EEPSEAL). Seismic acquisition has been completed in both blocks. Data is currently under processing and interpretation to establish drilling locations in each block. EEPSEAL will next undertake drilling of wells, expected to commence by year end 2007.

**Planning for the future**

Your Company has begun the implementation of the up-gradation of base refinery by addition of the following units i.e. Delayed Coker, VGO Hydrotreater, second Diesel Hydrotreater (High Pressure), ATF Hydrotreater and three small units Amine Regeneration Unit, Sour Water Stripper Unit and ATF Merox Units. This will enable the Refinery to process very heavy and sour crudes to produce products meeting exacting current international standards. In petroleum terminology this would translate into increasing the “Nelson’s complexity index from 6 to 12". Simultaneously, the Company would also be de-bottlenecking the primary units (CDU/VDU) which will increase the refining capacity to 16 MMTPA. All these actions are expected to have a significant positive impact on margins.

World renowned Technology providers and consultants, UOP have completed the configuration study with the objective of processing heavy, sour crudes to produce international quality petroleum products while expanding minimum energy and protecting and preserving our environment. Your Company has already executed contracts with key process licensors (UOP, Jacobs and ABB) who have made significant strides in completing the Basic Engineering work for these Units. Contracts have also been executed for Detailed Engineering, Procurement of Equipment and Construction of the Refinery, and the Contractors have received firm bids for equipment with long lead delivery periods. The cost of the proposed expansion and up-gradation is estimated at USD1.2 billion and is proposed to be funded with a debt to equity of 2.85:1. The Company has targetted to complete the expansion project by December 2009.

**Financial Highlights**

Your Company earned a total income of Rs 484.37 crore in the twelve months ended 31st March 2007 as against Rs 699.22 crore in the twelve months ended March 31, 2006. The under-recoveries in the marketing of transport fuels on account of Government’s retail pricing policy forced the Company to further curtail its sales during the year, resulting in steep decline in total income. This has helped your Company to contain the loss before tax excluding non-recurring other income to Rs. 64.94 crore in the twelve months ended 31st March, 2007 as against Rs 154.64 crore in the corresponding period last year.

**Internal Control System**

Your Company has a proper and adequate internal control system commensurate with its size and nature of operations to provide reasonable assurance that its assets are safe guarded against significant misuse or loss. This is effectively supported by SAP, a Enterprises Resources Planning software, through which the Company ensures that all material business transactions are properly authorized, recorded and reported. Further, the utilization of funds for the Refinery project and its progress continues to be monitored by an independent and reputed accounting firm and by an international engineering firm respectively on behalf of the lenders.

The Company has a proper budgetary control system to monitor capital related as well as other costs, against approved budget on an ongoing basis. The significant observations made by internal auditors and other agencies on the control system and procedures are reviewed and remedial measures taken, wherever required. These are periodically brought to the notice of the Audit and Governance committee for their review and recommendations, if any.

**Human Resources**

Your Company views its employees as valuable resources and important stakeholders in the growth, prosperity and development of the organization. The Company is committed to creating an appropriate climate, opportunities and systems to facilitate identification, development and utilization of their full potential. Various talent management initiatives like motivational campaigns, Employee Assistance Programs, family bonding activities etc., have been undertaken to promote a stress-free environment to enable employees to enhance their efficiency and productivity and at the same time enjoy a better quality of life.

There were 1542 employees, mostly professionally qualified, on the rolls of the Company as on 31st March, 2007. As a part of the HR planning process, your Company has developed well-established systems for identifying training