

**Chapter IV**  
**Pricing of IMFL and FL**



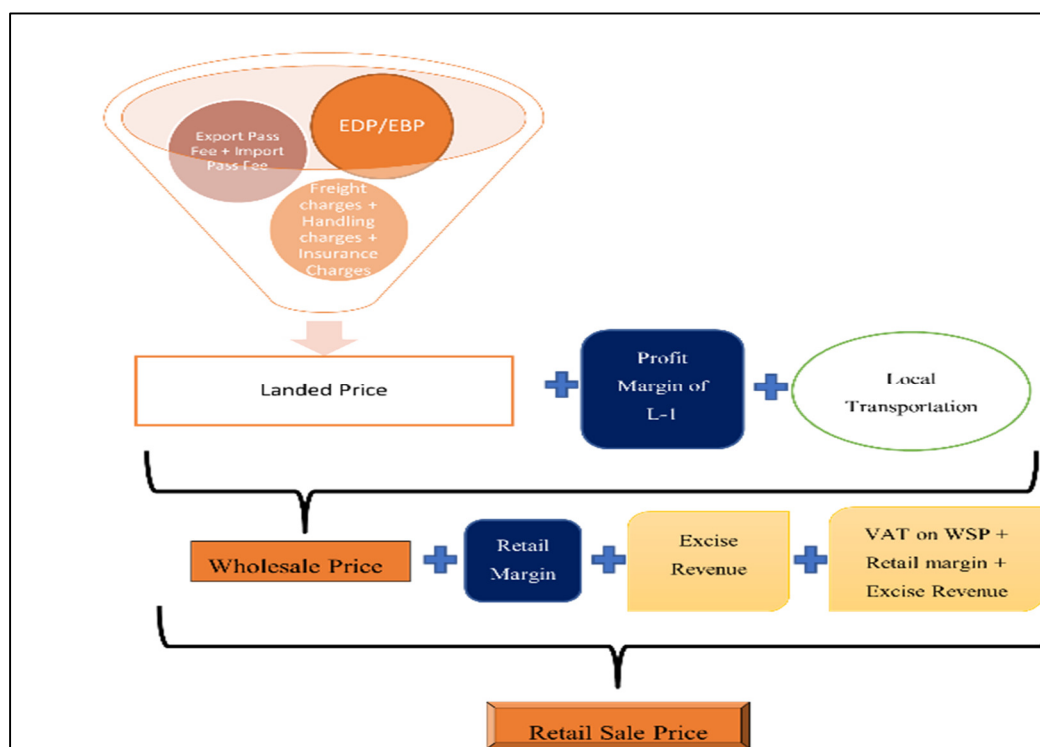
## Chapter IV: Pricing of IMFL and FL

*Pricing of liquor is highly sensitive and key determinant in regulating consumption, ensuring fair competition among suppliers and optimizing the Excise Revenue collection. Maximum Retail Price (MRP) is determined by the Excise Department based on initial cost inputs from the wholesale licensee and subsequent addition of Excise duty and VAT on fixed percentage basis while making allowance for profit margins. It was observed that the Government did not seek costing details to ascertain the reasonability of EDP/EBP.*

### 4.1 Introduction

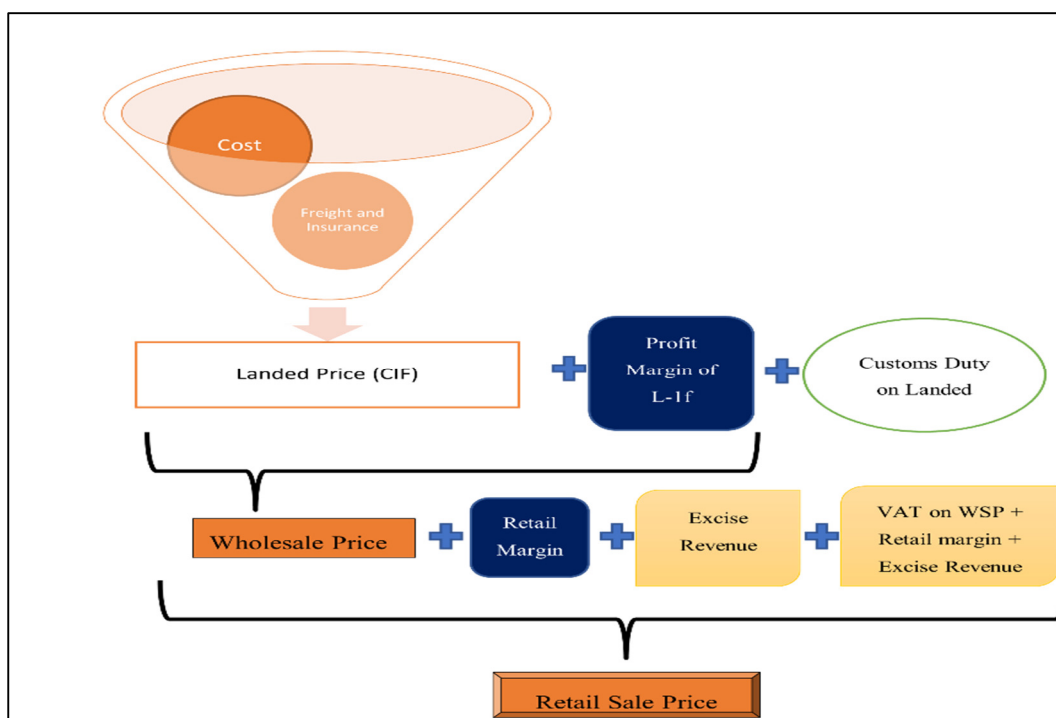
As per the Excise Policies for the years 2017-18 to 2020-21, the methodology adopted for pricing of IMFL is as given in **Chart 4.1**. In the pricing of IMFL, primary variable factor is its Ex-Distillery Price (EDP)/ Ex-Brewery Price (EBP). Profit margins/Duty/Taxes etc. are allowed/levied as a percentage of EDP/EBP.

**Chart 4.1: Cost Components of IMFL**



In respect of Foreign Liquor (FL), pricing methodology as depicted in **Chart 4.2** is slightly different. Unlike IMFL, where export fee is charged by the State where distillery is located, and import fee is charged by GNCTD, Customs Duty is levied by Government of India on Foreign Liquor.

**Chart 4.2: Cost Components of Foreign Liquor**



On scrutiny of records related to regulation of prices of IMFL by the Excise Department, Audit observed the following issues:

#### **4.2 EDP/EBP of IMFL not regulated by Excise Department**

Profit margin of L1 licensee is provided for separately by the Excise Department. Thus, the declared EDP/EBP should be based on actual cost components and other margins and should not be left to the discretion of the licensee. However, L1 licensee was at liberty to determine EDP/EBP at its discretion as per the Excise Policies of GNCTD.

Government replied that the approved Terms and Conditions for grant of L1 licence did not mention the use of cost criteria. It was also mentioned that in the new Excise policy, EDP would be declared on the basis of lowest EDP allowed in any State across India and an affidavit, in this regard, would be sought from licensees.

The reply is unsatisfactory as the concept of EDP is undefined and ambiguous. The issues arising from the use of EDP as the basis of pricing is discussed in the subsequent paragraphs.

##### **4.2.1 Reasonability of EDP/EBP not ascertained**

At the outset, it might appear that increase in EDP/EBP will increase the Excise revenue as well. However, the increase in EDP affects the MRP, which also carries the risk of decrease in sales which in turn can lead to loss of Excise revenue. However, as the Government did not seek costing details to ascertain the reasonability of EDP/EBP, there was a risk of L1 licensee getting compensated by the profits hidden in increased EDP/EBP.

Audit analysed EDP/EBP of brands of test-checked 11 licensees for the period 2017-21. In respect of the brands whose EDP was increased during this period, in majority of the cases excise revenue declined. It was noticed that the net effect on the excise revenue was a reduction of ₹ 165 crore in all the cases where the EDP was increased. Details are given in **Annexure VI**.

Discretionary power to declare EDP may lead to price variation in neighbouring states which has the potential to promote smuggling.

Government replied that brands above a certain MRP threshold were free to declare its EDP. It also mentioned that three highest selling whisky in terms of volumes are those with free EDP, suggesting that lower MRP due to restricted EDP does not *per se* determine the popularity of liquor. It further mentioned that the policy has been changed in new Excise policy for the year 2021-22 to make the minimum EDP uniform for all brands.

The reply is not satisfactory as the popularity of a brand cannot be correlated with its price only. The sales of a brand is sensitive to price changes at least to some extent, which itself is derived from the EDP. Thus, the EDP becomes an important parameter which must be regulated effectively.

***Recommendation 4.1: Ex-distillery Price should be defined along with all cost components and it may be clarified whether it includes any component of profit. Also discretionary EDP should not be allowed.***

#### **4.2.2 Fixation of higher EDP/EBP in Delhi than in other States**

As per the Excise Policies for the years 2017-18 to 2020-21, L1 licensee needed to keep the lowest EDP/EBP in Delhi for Whiskey/Wine with MRP upto ₹400, Rum/Gin/Vodka/Brandy with MRP upto ₹250 and Beer with MRP upto ₹100 (MRP in Delhi). Whereas, they had discretion to determine the EDP/EBP of brands with MRP above this limit.

Audit analysed the impact of discretionary EDP/EBP of brands with MRP above the limit. On detailed analysis of EDP/EBP of all 14 brands of the three L1 licensees who had provided the requisite details, it was observed that seven brands had lower EDP/EBP in other States than in Delhi.

**Table 4.1: Extra benefit to L1 Licensees**

Year	Brand	L1 Licensee	EDP in Delhi	Lowest EDP (State)	Excess EDP in Delhi	Sale in Delhi	Extra benefit to Licensee
2017-18	Royal Green Deluxe Blended Whiskey	M/S ADS Spirit	1323	1260 (Uttarakhand)	63	7,03,515	4,43,21,445
	Generation Deluxe Blended Whiskey	M/s ADS Spirit	2969	2689.31 (Jharkhand)	279.69	2,135	5,97,138
	Old Habit Rum	M/s Empire	899	780 (Kerala)	119	95,135	1,13,21,065
	Old Habit Vodka	M/s Empire	1089	902 (Kerala)	189	27,005	51,03,945

Year	Brand	L1 Licensee	EDP in Delhi	Lowest EDP (State)	Excess EDP in Delhi	Sale in Delhi	Extra benefit to Licensee
	Old Habit Whiskey	M/s Empire	1327	1125 (Kerala)	202	46,551	94,03,302
	Carlsberg Elephant Strong Super Premium Beer (500 ml)	M/s Mohan Goldwater Breweries Ltd.	724	533 (Daman)	191	73,020	1,39,46,820
	Carlsberg Elephant Strong Super Premium Beer (650 ml)	M/s Mohan Goldwater Breweries Ltd.	461	419 (Daman)	42	1,61,432	67,80,144
2018-19	Royal Green Deluxe Blended Whiskey	M/S ADS Spirit	1323	1305 (Goa)	18	11,05,225	1,98,94,050
	Generation Deluxe Blended Whiskey	M/s ADS Spirit	2969	2688.96 (UP)	280.04	4550	12,74,182
	Carlsberg Elephant Strong Super Premium Beer (500 ml)	M/s Mohan Goldwater Breweries Ltd.	857	533 (Daman)	324	26901	87,15,924
	Carlsberg Elephant Strong Super Premium Beer (650 ml)	M/s Mohan Goldwater Breweries Ltd.	525	419 (Daman)	106	75426	79,95,156
2019-20	Royal Green Deluxe Blended Whiskey	M/S ADS Spirit	1518	1305 (Goa)	213	10,39,194	22,13,48,322
<b>Total</b>							<b>35,07,01,493</b>

This mechanism carried the risk of L1 licensees including their profit in the inflated EDP as the profit margin was otherwise capped by Excise Department at five *per cent* while leaving the EDP/EBP largely unregulated.

The above table indicates that extra benefit to the extent of ₹ 35.07 crore was given to L1 licensees.

Government in its reply reiterated the point stated in para number 4.2.1.

***Recommendation 4.2: Government should review its pricing policy to effectively regulate the prices and maximize the revenue.***

### **4.3 Discretionary profit margin to Foreign Liquor licensees**

In case of Foreign Liquor, Government adopted a very liberal policy as L1F licensee was at liberty to determine its profit margin at its discretion.

Audit noticed that the profit margin of three test checked L1F licensees ranged from 44 *per cent* to 347 *per cent* of the Landed Price, and the average of percentage of profit margin to landed price was 255, 243, 169 and 172 *per cent* during the years 2017-18, 2018-19, 2019-20 and 2020-21 respectively. This resulted in inflated MRP for Foreign Liquor despite very low cost of import.

The influx of liquor through porous borders, owing to the price differential has also been highlighted by the Ravi Dhawan Committee formed (2020) by GNCTD to suggest measures for Excise Policy reforms. As per the Excise policy and license

requirement, the L1F (FL licensees) need to declare the WSP of all other States in which it supplies liquor. Audit observed that this condition was flouted, however, no objection was raised by the Excise Department itself (as discussed in **Paragraph 3.10**).

Government in its reply stated that WSP for FL has been fixed, since 2019-20, based on lowest WSP across India. It was further stated that market is dynamic and prices are regulated as per adjacent States' pricing. It was also mentioned that since the Excise duty on FL was 85 *per cent*, thus any increase in price would only help increase the Excise duty. It was also mentioned that since the market share of FL is 2.5 *per cent*, thus it does not have much impact on revenue. The reply further stated that the excise duty figures reported for the last three years shows increase in revenue. The reply regarding increase in excise revenue should be seen in the light of the fact that from 2019-20 to 2021-22, excise revenue increased by 8.28 *per cent* whereas, from 2016-17 to 2018-19, excise revenue increased by 18.27 *per cent*.

#### **4.4 Conclusion**

The basic premise of Ex-Distillery price of IMFL was undefined. Excise Department fixed the profit margin at five *per cent*, while leaving the EDP/EBP largely unregulated. This had a risk of the L1 licensees hiding their profits in EDP/EBP especially as the Excise Department did not ask for costing details. The pricing policy needs to have a more transparent basis.

