

Executive Summary

Background

Five factories of Ordnance Equipment Group (OEEG) under the control of Ordnance Equipment Group Headquarters Kanpur (OEF HQ) and Ordnance Factory Board Kolkata (OFB) are engaged in production of general stores and clothing (GS&C) items to meet the requirements of the Services. Army is the main recipient of these items (around 77 per cent).

Mention was made in previous Audit Reports of the Comptroller and Auditor General of India about inefficient production planning, deficiencies in procurement of stores and machinery, underperformance in production, underutilisation of resources, *etc.* in OEEG. Performance of these factories for the period 1999-2004 had been reviewed in audit during February-June 2004 and the results thereof were included in Paragraph 8.2 of Report No. 6 of 2005 of the Comptroller and Auditor General of India. The performance of OEEG was reviewed by us afresh during January - July 2011 with focus on the areas of production planning, utilisation of capacity, production and issue of GS&C products of specific quality at the right time to the Army (major recipient of the products). The data for the year 2011-12, wherever stated in this Report, was collected subsequently in April 2013.

The Performance Audit of these factories for the years 2008-12 brought out systemic deficiencies right from planning to execution.

Key findings

1. Shortcomings in fixation of annual production targets

Deficiencies including mismatch of the targets and capacity of the factories, delay in fixation of targets for annual production and subsequent unilateral reduction of targets by the factories persisted, which resulted in slippages in supply of items to the Army.

(Chapter-III)

2. Violation of procurement norms

Paragraphs 3.1.1, 3.7.7, 4.6.1 and Annexure-47 of OFB's Material Management and Procurement Manual (MMPM) stipulate the procurement norms, procedures etc. We observed that procurement of stores in violation of these extant provisions in MMPM resulted in over-provisioning of stores worth ₹165.54 crore during 2008-11. Similarly, against the prescribed

provision for 20 *per cent* purchases through open tender enquiry (OTE) in MMPM, four factories, in violation, made only 4 to 10 *per cent* of the purchases through OTE. An extra expenditure of ₹12.31 crore was observed in procurement of 14 items through 40 supply orders due to limited tender enquiry (LTE), instead of OTE. Further, in violation of OFB's direction (April 2007), 107 supply orders valuing ₹94.33 crore were placed by OEFG even though the rates exceeded the reasonable limit of eight *per cent* over the last purchase rate. This manifests that reasonability of rates was not ensured before placing orders by the factories.

Failure to break the suppliers' cartel in line with the OFB's instruction of July 2007 led to procurement of stores worth ₹33.91 crore through 102 orders from different suppliers, at identical rates.

As compared to the specific timeframe stipulated in MMPM, there were significant delays (up to 1441 days) in placement of 4117 orders valuing ₹430.63 crore, out of 11689 orders placed by the five factories in 2008-12.

(Chapter-IV)

3. Slippages in production and issue of items to the Army

In 116 out of 208 instances, the percentage of shortfalls in production and issue of GS&C items to the Army ranged between 21 and 100. The value of shortfalls in respect of 34 to 41 items out of 52 items analysed each year works out to ₹1147.13 crore during 2008-12. Besides, the value of issues to the Services spilled over to the next year amounts to ₹493.08 crore. The endemic slippages in issue of GS&C items despite outsourcing of jobs and unilateral reduction of targets in many cases, caused serious concern to the Army. OEFG also failed to tap the potential needs of paramilitary forces as it catered only 2.62 *per cent* of their requirements (₹1068.36 crore) of GS&C items during 2008-12.

(Chapter-V)

4. Underutilisation of resources

Although the available standard man-hours was not fully utilised, the factory managements allowed overtime payments of ₹48.68 crore to the Industrial Employees (IEs) in excess of actual requirement in 2008-12. Besides, the factories made additional payment of ₹10.91 crore towards piece work profit to IEs in 2011-12. Use of machines on single shift also led to underutilisation of capacity in the range of 45 to 69 *per cent*.

(Chapter-VI)

5. Poor quality control and assurance of products

Inefficient manufacture and inadequate quality control by the factories led to increasing trend of 'Returned for Rectification' (RFR) at quality assurance stage even in respect of established items. High level of RFR beyond 20 *per cent* and up to 100 *per cent* was noticed in 72 out of 266 instances in respect of 31 items during 2008-12. There were final rejections of five items valuing ₹11.66 crore in two factories during 2009-11. Apart from regular customer complaints, we came across rejections worth ₹10.42 crore in five cases at the users' end though the same were passed in inspection by Quality Assurance agencies.

(Chapter-VII)

6. Recurring loss in issue of products to the indentors

Deficient pricing mechanism of OFB and ineffective cost control by the factories led to recurring losses in four factories during 2008-12 in issue of items to the indentors. Net loss suffered by the OEFG worked out to ₹226.09 crore during 2008-12. Besides, there was extra expenditure of ₹105.47 crore in 16 instances due to higher cost of production for common items at one factory compared to that of another factory. OEFG had the production share of only six *per cent* every year while it accounted for 16 to 18 *per cent* of direct labour cost of ordnance factory organisation as a whole during 2008-12. OEFG could not tap potential market for its products due to their exorbitant price.

(Chapter-VIII)

7. Ineffective internal control and monitoring

Inadequate internal control and lack of proper monitoring at the factories coupled with ineffective monitoring and guidance by the OEF HQ resulted in irregular booking of labour charges on closed/non-existent warrants, non-regularisation of losses arising from rejections/wastages and manufacture with excess or without drawal of material. The monitoring by the top level management on the working of OEFG was also inadequate.

(Chapter-IX)

Recommendations

- *Ministry may ensure that the Army and OFB, in close coordination, fix production targets taking into account Army's requirement and capacity of OEFG. OFB should communicate its production capacity for each item to the Army well in advance before target fixation meetings.*
- *Ministry may ensure that the Army and OFB hold target fixation meetings at the appropriate time so as to give the factories the required procurement lead time.*
- *OFB may ensure that the factories adhere to the prescribed policy/guidelines in assessment of net requirement of stores for reliable and accurate provisioning to avoid excess procurement.*
- *The e-procurement system should be implemented effectively in all the factories and all factories should maintain shareable database.*
- *OFB may ensure that the procurement agencies strictly adhere to the OFB's guidelines of July 2007 to prevent cartelisation.*
- *Ministry may ensure that OEFG formulate judicious production and procurement plan so as to achieve realistic production targets.*
- *A system should be institutionalised to ensure that Army's account is debited with simultaneous credit of ordnance factories' account only after the stores are inspected and cleared by the consignee Army's depots to plug the deficient accounting for spill-over issues.*
- *OFB may streamline the outsourcing policy to minimise the outsourcing of jobs so as to ensure optimum capacity utilisation and also institute a mechanism to ensure reasonableness of rates.*
- *OFB should generate a database at OEF HQ with the latest and reasonable rates for outsourcing of jobs which can be shared by all factories.*
- *OFB may ensure that the factories plan their production activities efficiently, deploy their manpower judiciously in tune with the workload requirements and fully utilise the available SMH before resorting to work on overtime payment.*

- *Ministry may ensure that OFB follow the correct methodology for making payment towards piece-work profit by excluding additional 25 per cent over and above the output SMH booked.*
- *OFB should operationalise two-shift working in the factories to increase the productivity and to optimise capacity utilisation.*
- *OFB should put in place a system of periodical review of inventory holding at different factories as well as take prompt action to dispose of all surplus/obsolete/non-moving/waste after proper identification.*
- *OFB must ensure that the factories diligently follow the prescribed norms for inspection of input materials.*
- *OFB may ensure that factories adhere to 100 per cent pre-inspection as required, by independent Quality Control staff of the factories.*
- *Ministry may ensure that OEFG generate reliable cost-data for enforcing strict cost control on the products.*
- *Ministry may ensure that the OFB and the factories strengthen their internal controls and monitoring mechanisms, especially in planning and production, accounting and documentation of the related activities.*
- *A comprehensive and effective internal control system must be put in place by the OEFG to avoid irregularities in booking of labour charges and manufacture with excess or without drawal of materials.*