

Chapter V: Production Performance

Audit objective

Whether the factories efficiently produced items as per annual production target and issued the same to the indentors within the financial year.

Source of audit criteria

- Monthly production reports; and
- Policy on outsourcing of jobs;

5.1 General

OEEG are responsible for meeting the requirements of GS & C items for the Services. Services resort to trade procurement/import of items, when the factories are unable to supply as well as for items⁷ which are not manufactured by the factories. During the period 2008-12, the Services resorted to trade procurement/import of items worth ₹2141.28 crore which constitute 44 per cent of total procurement by the Services from trade/import and OEEG. The details of trade procurement/import *vis-a-vis* intake from the OEEG by the Services during 2008-12 are tabulated below:

Table-12: Procurement by Services from trade *vis-a-vis* OEEG

(₹ in crore)

Services	2008-09		2009-10		2010-11		2011-12		Total	
	Trade	OEEG	Trade	OEEG	Trade	OEEG	Trade	OEEG	Trade	OEEG
Army	636.28	453.19	508.75	437.66	427.89	643.81	247.70	705.57	1820.62	2240.23
Air Force ⁸	60.82	119.94	59.40	92.02	15.88	87.85	56.78	101.24	192.88	401.05
Navy	20.67	9.34	19.86	9.20	45.47	10.93	41.78	19.92	127.78	49.39
Total	717.77	582.47	588.01	538.88	489.24	742.59	346.26	826.73	2141.28	2690.67

The comparison of supplies by OEEG against the trade procurement/import by the Services brings out that the OEEG were catering to only 56 per cent⁹ of the requirements of the Services. OEEG even failed to achieve the production targets relating to Army items in all the four years, as discussed in the subsequent paragraphs.

⁷ Special clothing items *viz.* Sleeping Bag, Jacket Down, Trouser Down, Gore tex suit, Gloves Outer, Gloves Inner and Rucksack 70 Ltr, etc.

⁸ Actual expenditure for clothing and general stores procured from trade by Air Force and Navy could not be obtained from Air/Naval HQ. Hence, data relating to the trade procurement of clothing stores for 2008-11 have been taken from Defence Services Estimates and data for 2011-12 obtained from Ministry of Defence (Finance) Budget Division.

⁹ Calculation : $\frac{\text{Procurement from OEEG} \times 100}{\text{Procurement from Trade} + \text{OEEG}} = \frac{2690.67 \times 100}{4831.95} = 56 \text{ per cent}$

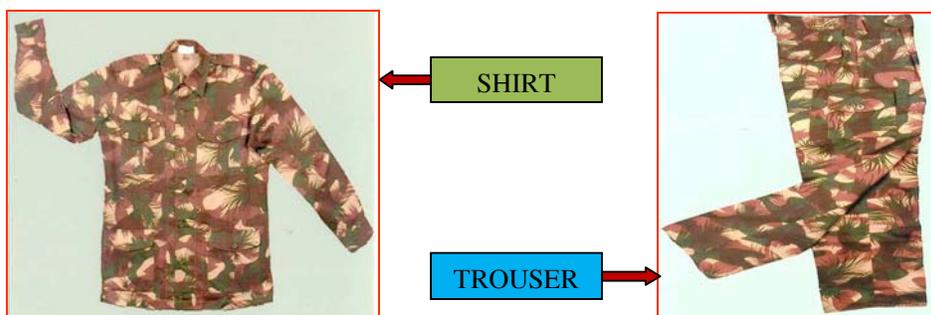
5.2 Shortfall in production/issue against targets

The details of item-wise target, production and issues reported by the OEF HQ, shortfall in issue and value of shortfall in respect of 52 items during 2008-09 to 2011-12 are indicated in **Annexure-II**. The Annexure brings out shortfall in production/issue for 34 to 41 items valuing ₹1147.13 crore during 2008-12. Factories also failed to issue full quantity that had been produced, to the Army in respect of 15 items in 2008-09, six items in 2010-11 and five items in 2011-12. The table below summarises the number and range/value of shortfall in production and issue.

Table-13: Analysis of shortfall in production/issue

Year	Number of items analysed	Number of items where shortfall existed	Number of items			Total value of shortfall (₹ in crore)
			Range of percentage of shortfall			
			1 to 20	21 to 50	51 to 100	
2008-09	52	34	6	12	16	155.56
2009-10	52	37	4	10	23	447.90
2010-11	52	35	7	12	16	183.42
2011-12	52	41	14	7	20	360.25
Total						1147.13

The Central Ordnance Depot Kanpur (Army), in March 2010, expressed serious concern about critical deficiency of 13 items¹⁰ due to non-supply/short supplies by the OEEG during 2009-10. Against the target of 4,87,444 Boot High Ankle DVS, OEFC could supply only 32,500 boots in 2009-10 as evident from **Annexure-II**. This forced OEF HQ to issue no objection certificate to the DGOS for trade procurement of two lakh boots. Again, ADGOS (Clothing, Necessary and Administration) apprised (May 2012) Addl. DGOF, OEF HQ of serious slippages in production and supply of 41 items (₹169.98 crore) against the mutually accepted targets for 2011-12.



¹⁰ Net mosquito, Shirt PW PV DD OG, Durries, Boot high ankle DVS, Boot Paratroopers, Jersey woollen V neck, Cover water proof(4 types), Fly outer 4M, End curtain, Fly outer 2M.

The slippages were mainly due to delayed finalisation of firm targets, acceptance of targets beyond the capacity for some product-mix, slippages in procurement of stores and low utilisation of capacity.



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The Ministry attributed the shortfall in production to delayed fixation of firm target by DGOS and OEF HQ and delay in giving size-wise distribution by DGOS, delayed placement of order, inadequate supply of raw materials - mainly garniture items, delayed clearance of final product in inspection by DGQA and acceptance of target beyond capacity for certain items.

The reply of the Ministry is an admission that the reasons for slippage and low capacity utilisation were attributable to known factors which should have been appropriately addressed. Moreover, the reply is silent on the remedial action proposed to be taken.

5.3 Spill-over production/issue

According to Paragraphs 668 and 670 of Defence Accounts Department Office Manual Part-VI (DAD OM), the manufactured items are accepted after inspection and thereafter, the accepted items are brought on charge in the Production Ledger. Subsequently, those items, when issued to the indentors through production issue vouchers are priced with reference to OFB's firm price list and accordingly, debited to the relevant Services' head.

Items which are neither manufactured nor physically issued by 31 March of a financial year, but 'shown as issued' to the indentors in the accounts of Ordnance Factories, are termed as 'spill-over' production/issue. This leads to reporting of inflated issues in the factories' accounts and release of payment from the Services' accounts without physical receipt of the stores from the factories.

The Controller General of Defence Accounts (CGDA), New Delhi had informed (October 2007) all Controllers of Finance and Accounts (Factories)¹¹ that advance issue vouchers were being prepared by Ordnance Factories without any physical issue of stores to the Services in order to take payment from the Services. CGDA also impressed that this deficiency resulted in many accounting irregularities (depiction of unrealistic profit in the accounts, distortion of cost of production and work-in-progress, disparity between value of issues and actual expenditure booked under manufacturing head, etc).

In order to end this irregularity, the CGDA instructed all Controllers of Finance and Accounts (Factories), in October 2007, not to accept advance issue vouchers without despatch particulars for financial adjustment.

However, all the five factories did not follow the instructions and continued to resort to 'spill-over' production/issue, which had aggregated to ₹493.08 crore during 2008-12, representing 18 per cent of the total issues to the Services, as detailed below:

Table-14: Factory-wise value of spill-over issue

Factory	Value of spill-over items (₹ in crore)				Total (₹ in crore)
	2008-09	2009-10	2010-11	2011-12	
OEFC	84.81	69.10	58.97	Nil	212.88
OPF	Nil	28.55	10.54	Nil	39.09
OCFA	21.05	20.19	6.34	Nil	47.58
OCFS	47.80	28.20	37.43	55.32	168.75
OEFH	Nil	14.43	3.84	6.51	24.78
Total	153.66	160.47	117.12	61.83	493.08
Percentage of total issues	26	30	16	7	18

The Secretary, Defence Production assured the *Raksha Mantri* in January 2011 that there would be no spill-over in production during 2010-11. Despite this assurance, we observed significant quantum of spill-over issues worth ₹117.12 crore in 2010-11 and ₹61.83 crore in 2011-12.

While accepting the facts and assuring to stop spill-over in future, OFB, in April 2012, stated that the following factors were responsible for spill-over production:

¹¹ Controller of Finance and Accounts (Factories) functions under the PCA (Factories) Kolkata for a group of factories on regional basis.

- Delayed target fixation and placement of indents by all indentors;
- Late receipt of size-wise details mainly from the Army; and
- Delay in procurement action resulting in non-availability or late receipt of raw materials.

The above mentioned factors, however, did not justify the accounting of advance issues without corresponding physical production and issues.

5.4 Outsourcing of jobs

The factories are allowed to get trade assistance/outsourcing of jobs, wherever in-house manufacturing capacity is not sufficient to meet the targeted production. The Chairman, OFB, while expressing the need for quality improvement, instructed all factories in May 2008 that production of uniforms ordered on the OFB should not be outsourced.

However, we observed that during 2008-12, ₹159.93 crore was spent on outsourcing of fabrication jobs on various items including uniforms (₹9.63 crore). We also observed other irregularities and lapses in outsourcing of jobs on the grounds of capacity constraints with reference to inflated targets, unjustified outsourcing despite availability of sufficient in-house capacity and outsourcing without adhering to quality and security aspects. Even with outsourcing, the targets were not met as discussed below.

5.4.1 Outsourcing due to acceptance of target beyond capacity

As discussed in Paragraph 3.3.1, OEF HQ accepted target beyond the available capacity in respect of 7 to 16 items during 2008-12. Resultantly, OEFG resorted to trade assistance with the approval of Addl. DGOF and Chairman, OFB. The details of outsourcing of a few items in 2008-09, 2009-10 and 2011-12 are indicated in Table-15.

Table-15: Trade assistance due to high production target

Item	Capacity (in number)	Final target (in number)	Percentage of excess target	Trade assistance		Issue (in number)
				Quantity (in number)	Value (₹ in lakh)	
OPF (2009-10)						
Fly Outer of Tent 2M	4000	15343	284	16678	27.15	5343
Shirt PW PV DD OG	100000	200000	100	50000	7.74	80000
Trouser PW PV DD OG	150000	200000	33	50000	8.32	100000
OEFC(2008-09)						
Boot High Ankle DVS						
i) Fabrication Operation	500000	500000	Nil	100000	403.28	400000
ii) Clicking Operation	225000		122	140000	12.32	
iii) Lasting Operation	420000		19	100000	27.00	
iv) Moulding Operation	600000		Nil	108000	49.63	
OEFC (2009-10)						
Boot High Ankle DVS						
i) Clicking Operation	225000	487444	117	150000	15.12	32500
ii) Moulding Operation	600000		Nil	36000	16.54	
OCFA (2009-10)						
Trouser PW PV DD OG	100000	500000	400	133334	68.00	100000
Liner inner (TEFS 4M)	Nil	12000	@	8000	N.A.	6120
Overall Navy Blue	Nil	3248	@	3248	N.A.	3248
OEFH*						
All items (2009-10)	13.40 lakh SMH	39.91 lakh SMH	198	1.63 lakh SMH	31.03	14.51 lakh SMH
All items (2010-11)	13.75 lakh SMH	19.92 lakh SMH	45	7.19 lakh SMH	142.04	14.29 lakh SMH
OCFS (2011-12)						
Jacket Wind Cheater	30000	54000	80	9090	5.00	18200
Trouser Wind Cheater	30000	49000	63	50000	14.99	18400
Total					828.16	

@Not determinable as no specific capacity was mentioned.

* Item-wise details not available, hence figures given in labour hours (SMH)

The foregoing table indicates that the trade assistance sought by the factories for certain selected items was substantial and amounted to ₹8.28 crore.

The Ministry's response and our comments thereon are indicated in Table-16.

Table-16: Ministry's response and Audit remarks

Ministry's response	Audit remarks
There was no scope of non-acceptance of target when fixed by OEF HQ even beyond factory's capacity.	The reply indicates that capacity of factories had not been properly assessed upfront by the OEF HQ nor was the matter of allotting the targets beyond the capacity taken up by the factories with OEF HQ. This led to recurring events of trade assistance.
Trade assistance was resorted to at cheaper cost in case of urgent requirement and capacity constraints.	Outsourcing on the plea of lesser labour cost compared to factory cost flags the question of efficiency of the factory.
Trade assistance was sought for labour oriented operations only.	
Completion of targets through trade assistance depends on availability of raw material, readiness of cut components and garniture items ¹² .	Non-achievement of targets despite trade assistance points to the factory's failure to position the input materials in time.

¹² Items relating to decorative accessories for beautification

5.4.2 Outsourcing despite availability of sufficient in-house capacity

We observed that despite sufficient in-house capacity, two factories outsourced jobs valuing ₹11.05 crore to trade during 2009-12. Even after trade assistance these factories failed to meet the production targets in most of the cases. Details of item-wise capacity, target, trade assistance and final issue are shown in Table-17.

Table-17: Trade assistance despite in-house capacity

Item	Capacity	Target	Trade assistance		Issue
			Quantity	Value(₹ in lakh)	
OCFS (2010-11)					
Coat ECC	50000	50000	35000	224.00	25000
Cap FS	150000	100000	300000	38.40	10000
Jersey DBG/V OG	260000	245000	21000	17.85	235000
Blanket	400000	350000	80000	493.12	260000
OCFS (2011-12)					
Coat ECC	80000	80000	59018	309.84	27000
OCFA (2009-10)					
Overall Greenish Khaki	41425	41425	35000	22.05	41425
Total				1105.26	

Response of the Ministry and our comments thereon are indicated in Table-18.

Table-18: Ministry's replies and Audit comments

Ministry's response	Audit remarks
Outsourcing orders were placed at a belated stage only after review of the balance workload <i>vis-à-vis</i> capacity available. Due to non-availability of some basic materials and garniture items, supplies could not be achieved as per target.	Reply is not specific to the audit findings in regard to outsourcing the jobs despite sufficient in-house capacity. Systematic review and assessment of workload <i>vis-à-vis</i> availability of manpower and materials were not done by the factories to ensure the timeliness and exact requirement of outsourcing.

5.4.3 Outsourcing without enforcing quality and security deposit

While according approval of trade assistance sought by the factories, OEF HQ generally stipulates the following conditions:

- Compliance with applicable rules and provisions of Procurement Manual should be ensured;
- Cost of trade fabrication should be less than the factory's cost for the same operation;
- Cut components and garniture items are to be supplied by the factory;
- Quality control is to be ensured by the factory; and
- Production target is to be completed by 31 March each year.

Detailed scrutiny of the fabrication orders revealed the following irregularities:

- OFB's MMPM stipulates that General Managers are required to obtain security deposit equal to book value of the stores issued to the contractors from factory's stock plus 10 *per cent* on the all inclusive cost of the order. However, OPF handed over cut components worth ₹5.98 crore to the contractors for fabrication of fly outer for tent, uniforms, *etc.*, without obtaining the required security deposits from the contractors, in respect of 10 fabrication orders during 2009-10;
- OCFA received 99,466 trousers (PV DD OG) against 1,33,334 ordered in three fabrication contracts of December 2009 with reference to the production target of five lakh trousers in 2009-10. Out of the supplied quantity, 27,202 trousers were found defective in COD Kanpur and the factory was forced to send its team to rectify the defects; and
- There were delays and short supplies of items from the trade firms in respect of 61 orders (80 *per cent*) out of 76 orders analysed in respect of OPF, OEFH and OEFC which ultimately defeated the condition of meeting the production target within the financial year.

Ministry/OFB's replies and our comments are in Table-19.

Table-19: Ministry/OFB's replies and Audit comments

Ministry/OFB's reply	Audit comments
OPF obtained indemnity bond from the firms as guarantee of the materials issued to them for fabrication work.	As the indemnity bond was not issued by any financial institution/bank, it cannot be treated as adequate safeguard of Government property.
Outstanding supplies received at belated stage was gainfully utilised to meet next year's target at OEFH.	OFB's replies indicate failure of the factory management to get the fabrication orders executed by trade in time.
Late supply of raw materials by OEFC to trade led to delayed execution of fabrication orders by trade.	The reply is silent as to what corrective action was taken to avoid late supply of raw materials to the trade.
OCFA achieved the target of 1 lakh trousers PV DD OG and supplied these to COD Kanpur in 2009-10.	OFB's reply regarding OCFA is not acceptable as target was for supply of 5 lakh trousers. Reply did not explain why the defective trousers were sent to COD Kanpur, without proper inspection.

5.4.4 Fabrication orders placed at uneconomical rates

Our comparison of rates for execution of fabrication jobs by factories showed that the rates accepted by OCFA were substantially higher by as much as 234

per cent compared to that of other factories for the same job, resulting in extra expenditure of ₹2.14 crore against 25 orders, as depicted in Table-20.

Table-20: Inter-factory comparison of outsourcing rate for same job

Item	Outsourcing at higher rate by OCFA		Outsourcing/factory cost at lower rate		Extra expenditure (₹ in lakh)
	No. of orders & date	Quantity (Rate)	Order No. & date	Rate	
Fly outer TEFS 4M	4 orders dt. 19.02.09	1000 (₹1032)	263 dt. 19.06.09 (OEFC)	₹350	6.82
	3 orders dt.16.12.10	5000 (₹1032)	506 dt. 03.10.10 (OEFC)	₹408	31.20
Trouser PW PV DD OG	3 orders dt.24.12.09	133334 (₹51)	508 dt. 04.01.10 (OPF)	₹16.64	45.81
End curtain TEFS 4M	4 orders dt.20.09.08	8000 (₹927.50)	360 dt.19.08.08 (OEFC)	₹278	51.96
	2 orders dt. 03 and 13.12.11	10000 (₹721.50)	388 dt. 04.09.11 (OPF)	₹340	38.15
	1 order dt. 05.03.12	7500 (₹610)			20.25
Liner Inner TEFS 4M	6 orders dt.10.11.09	3000 (₹761)	454 dt. 08.09.10 (OEFC)	₹325	13.08
	2 orders dt.30.11.11 and 12.12.11	2200 (₹635)	198 dt. 11.11.11 (OEFH)	₹310	7.15
Total					214.42

Though OEF HQ accords permission for trade assistance yet they did not effectively monitor the reasonableness of rates in fabrication orders placed by different factories.

The Ministry stated that the rate accepted by OCFA was high being located at A-1 city. Higher labour cost at OCFA compared to OEFC/OPF cannot justify difference of fabrication cost in the range of 79 to 234 per cent.

5.5 Civil trade/export activities

OEEG undertook civil trade/ export activities since 1986 to utilise the spare capacity after meeting the requirements of the Services and established Regional Marketing Centres to explore prospective customers. Details of issues made to all civil indentors including Ministry of Home Affairs (MHA) and exports during 2008-09 to 2011-12 are indicated in Table-21.

Table-21: Factory-wise details of civil trade issue

Factory	(₹ in crore)			
	2008-09	2009-10	2010-11	2011-12
OEFC	0.64	12.13	5.72	0.03
OPF	0.53	0.78	1.55	0.98
OCFS	3.75	2.43	2.90	9.03
OEFH	0.67	5.12	0	1.24
Total	5.59	20.46	10.17	11.28

The table indicates that civil trade and export activities by OEFG were not significant. Total value of issues on account of civil trade and export reduced from ₹20.46 crore in 2009-10 to ₹10.17 crore in 2010-11. One of the reasons for the failure to tap potential market is the significantly higher rate of OEFG produced items. The Director General, Sashastra Seema Bal had informed us in July 2012 that the rates of OEFG produced items were as high as 300 *per cent* compared to market rates. The expenditure on procurement of GS&C items by the paramilitary forces during 2008-12 was ₹1068.36 crore, of which items valued at ₹27.95 crore (2.62 *per cent*) was sourced from the OEFG.

5.6 Audit conclusion

Even after outsourcing, targets were not met fully and we observed numerous slippages in production and issue of GS&C items by OEFG.

Recommendation 6

Ministry may ensure that OEFG formulate judicious production and procurement plan so as to achieve realistic production targets.

Recommendation 7

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.

Recommendation 8

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.

Recommendation 9

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.