

Defence Procurement Procedure 2013 – A leg up for indigenization?

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The Defence Procurement Procedure (DPP) 2013, released by the Ministry of Defence (MoD) on June 1, 2013, would be known for three important changes in the procedure that existed before its promulgation. First, the existing categories, under which the defence equipment is procured or manufactured, have been arranged in a hierarchical order. Two, what would actually constitute 'indigenous content' has been defined and the provisions regarding meeting this requirement have been made more stringent. Three, the maintenance technology will not have to be any longer necessarily transferred to the agency nominated by the Department of Defence Production. To be sure, some other changes have been made but these three changes are the most significant from the policy perspective.

The concept of categorization of the procurement proposals is not new. What DPP 2013 has done is to arrange them in a hierarchical order, starting with 'Buy (Indian)' category. This is followed by 'Buy and Make (Indian)', 'Make (Indian)', 'Buy and Make' and 'Buy (Global)' in a descending order of priority. What does it imply? Does it imply that if the MoD needs to buy any equipment it would first consider the possibility of buying from the Indian companies and if that option is not viable it would consider buying that equipment under the 'Buy and Make (Indian)' category? And, if that option is also not workable, would it then consider the 'Make (Indian)' option? And, so on.

That could not have been the intention behind the hierarchical arrangement of the procurement categories. Take, for example, a situation in which, for a variety of reasons, it may be sufficient to 'buy' an item, and not also to 'make' it in India. This may be due to the requirement being one-off or the required quantity being limited. This would imply that if no Indian company is in a position to offer that item, there would be no option but to resort to the 'Buy (Global)' category. Therefore, in a situation where some equipment is required only to be bought and not made in India, the choice would be between 'Buy (Indian)' and 'Buy (Global)'.

If, on the other hand, the equipment is required to be made in India, the choice would be between 'Buy and Make (Indian)' and 'Buy and Make', depending on a variety of factors. The intervening category of 'Make (Indian)' in the newly ordained hierarchy of procurement categories will not fit into the scheme of things because of the long gestation period of the projects under the 'Make (Indian)' category as such projects involve design, development and indigenous production.

For some time at least, the 'Make (Indian)' category is unlikely to be invoked. The procedure laid down in the DPP requires the Headquarters of the Integrated Defence Staff to have the projects categorized as 'Make' projects and obtain the Acceptance of Necessity (AoN). Since the time the 'Make' category was introduced in the DPP in 2006 probably only four cases have been categorized as 'Make' projects. In one of these cases (Futuristic Infantry Combat Vehicle), the Request for Proposal (RFP) has reportedly been withdrawn. The progress made in the remaining three cases does not inspire much confidence in the future of the 'Make' procedure.

Realizing that there are problems besetting the 'Make' procedure, the MoD has constituted a high level committee for suggesting how to simplify this procedure. It is difficult to understand why it took so long to set up a committee. The Defence Production Policy of January 2011 stated that the

Government will further simplify the procedures under the “MAKE” category in such a manner that it enables the indigenous design and development of the required equipment/ weapon systems/ platforms by both public and private industry in a faster timeframe.

Anyway, now that the committee has been set up, it is unlikely that any new project would be categorized as a ‘Make’ project till the procedure is simplified by the MoD based on the recommendations of the committee. This could take a while and, if past experience is anything to go by, the report of the committee could remain under consideration for a long time and the recommendations of the committee may remain unimplemented. In any case, there might not be very many projects that would qualify to be categorized as ‘Make’ projects.

The new hierarchical ordering of the procurement categories might, therefore, have little impact on promotion of indigenous procurement and production as the real indigenization would come only through the ‘Make’ procedure.

The second important change concerns the definition and assessment of the indigenous content in the equipment to be procured under various categories. The uncertainty about what constitutes indigenous content in a product has been removed by defining the concept in precise terms in DPP 2013. However, another complexity has been added by mandating that the minimum prescribed percentage of the indigenous content in the products is required not only in relation to the total value of the contract but also in regard to the basic cost of the equipment, cost of the manufacturer’s recommended list of spares (MRLS) and the cost of the special maintenance tools/test equipment taken together.

Compliance of this requirement will be monitored through compliance certificates given by the vendors/sub-vendors, though the MoD has retained the power of auditing such certification either on its own or through a nominated official or an agency. Every sub-vendor, up to the lowest level in the chain, will be required to inform the vendor up the chain of the indigenous content added in the assembly/sub-assembly at his level. While entering into the contracts with one another, the prime vendor and all sub-vendors will be required to include in the contract the requirement of reporting of the indigenous content to the immediately higher level integrators and audit by the MoD. This makes the situation cumbersome and prone to transgressions.

It has also been mandated that the prescribed minimum percentage of indigenous content should be present in the product when it is offered for trials. It remains to be seen if it would be possible for the Indian vendors to produce equipment for trials with a minimum of 30 per cent indigenous content.

The efforts to promote indigenization could run into some problem on these counts. In any case, the latter requirement might have only limited impact on indigenization. One cannot help wondering whether the objective of promoting indigenization would not have been served better by making a provision in the DPP that MoD would indicate in the RFP the specific area(s), related to a particular procurement programme, in which the vendor will have to ensure the minimum percentage of indigenous content. This kind of channelization of the effort at indigenization is likely to produce better results. A similar provision in the context of the discharge of offsets would have made a tremendous difference.

The third significant change made in DPP 2013 is in regard to transfer of maintenance technology. The incongruity between what the MoD's Press Release of June 1, 2013 states in this regard and the text of the relevant paragraph (No 28) in DPP 2013 notwithstanding, the intention of the MoD seems to be to let the foreign, as well as the Indian vendors, choose the Indian agency to which the maintenance technology could be transferred, rather than such an agency being nominated by the Department of Defence Production.

This opens up a huge opportunity for the private sector in India. Maintenance is not an insignificant low-value job, especially when it comes to big platforms like the aircraft. There is much to be gained from this opening that the MoD has provided. It would provide the Indian private industry the wherewithal not only to get into the maintenance segment but also help it in acquiring the capabilities which could be used as the springboard for venturing into manufacturing of defence equipment. It would also spare the manufacturing companies/integrators from the task of maintenance, thereby allowing them to concentrate on the core function of manufacturing and also afford them the luxury of venturing into research and development. The MoD will, however, need to see if the text of the relevant paragraph in the DPP reflects this intention correctly.

It would have been desirable to make a similar provision in regard to upgrades. The Defence Production Policy of January 2011 had proclaimed that, as far as possible, upgrades will be carried out by the Indian Industr. It also stated that the Defence Research and Development Organization, HQ Integrated Defence Staff, Services Headquarters, Ordnance Factory Board, Defence Public Sector Undertakings and the private sector will work in close coordination for continuous upgradation of systems. An opportunity seems to have been lost for implementing this decision as DPP 2013 does not apparently specify any procedure for farming out upgradation to the Indian industry.

The other changes made in the DPP relating to freezing of the Services Qualitative Requirements (SQRs) before the Acceptance of Necessity (AoN), enhancement of the financial powers of the Services for capital acquisition, reducing the validity of the AoN from two years to one year, doing away with short-listing of vendors by the Project Appraisal Committee in 'Buy and Make (Indian)' cases, etc. are unlikely to have a direct bearing on promotion of indigenization.

Indigenization of defence production has to be spearheaded by the Indian industry, both in the public and the private sectors. It also requires the involvement of the Micro, Small and Medium Enterprises (MSMEs). This calls for a coordinated approach as all these sectors have specific problems that cannot be resolved by the MoD alone. Broadly speaking, the problems relate to industrial licensing, taxation, level-playing field, foreign direct investment, formation of joint ventures and exports. These problems are only indicative of the quandary that the Indian industry has got itself into. This list does not include the woes of the MSMEs.

A two-fold strategy could help overcome these problems. On its part, the MoD needs to provide a forum for a free flowing exchange of views between the officials of the ministry and all other stakeholders. As a corollary to this, an empowered structure needs to be created in the MoD which could resolve the issues as they arise and not let them fester till they become sore. On a wider scale, a forum needs to be created, with participation from the ministries of defence, finance, commerce (which exercises administrative control over the Department of Industrial Policy and Promotion), MSMEs and any other ministry or organization (such as the Planning Commission) that may be relevant to resolving the issues related to promotion of the defence industry in India. This entity could also supervise the metamorphosis of the fledgling Indian defence industry into a robust defence industrial complex without letting it grow into a Frankenstein.

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