

DEFENCE CONTRACTS

Lecture - 2

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DEFENCE CONTRACTS

- Sleaze, corruption, lack of transparency
- Jeep scandal
- Bofors scandal, HDW submarine deal
- Kargil procurements
- Tehelka revelation
- GoM recommendations
- Kelkar committee
- Denel contract
- Dhirendra Singh committee
- Rafale contract
- Committee (2019): Make in India
- Role of CVC Vitthal
- Admiral Ram Das, Transparency International

JEEP SCANDAL: LOSS OF 18 LAKH

- Report of DADS (1954)
- Army inspection report that 155 jeeps were class IV (unusable), not wholly correct
- As per contract inspection in India limited to ensuring that the vehicles were in a running condition and no damage is transit.
- Mechanical inspection carried out by M/s. Lloyds
- Cancellation hasty and ill considered
- Association of Krishna Menon with Sri James Marshall Cornwall and Partners

BOFORS SCANDAL

- Contract in March 1980: \$285M, 410 guns
- Swedish National Audit (1987)- \$40M paid in commissions to middle men, \$1.48B
- Quattrocchi as Middle man
- Lifting of ban during Kargil war
- Price calculation (CST) not done properly
- Change in technical assessment by General Sunderji (Shoot and Scoot)
- Technology Transfer Document

SUBMARINE DEAL WITH HDW (1987)

- 1979: CCPA approved submarine to submarine killer, diving depth of 300m
- Technical committee: Swedish, Italian offer, pieced HDW- Diving Deptt. of only 250 metres
- Subsequent Delegation cleared HDW
- 7% commission paid to secure the Contract (1989)
- Failure to take a firm stand against HDW

INTER GOVERNMENT AGREEMENT

- Procurement for friendly foreign countries due to geo strategic advantages
- Would not follow classical DP procedures
- Equipment of proper technology and capabilities from a friendly country is identified while participants in joint international exercises
- Multiple source: Select one
- Large value weapon system/platform available lesser cost than original platform
- Strategic consideration, not necessarily L_1

JV, Brahmos

- Pool Resources for achieving a specific objective
- Each party responsible for profit, loss, cost
- No of parties involved, Scope: Geography, Product & Technology
- Contribution of each party
- Structure, Control & Management
- Brahmos: \$250 M: India 50.5%, NPOM 409.5%
- P 800 Cruise Missiles

RAFALE DEAL CONTROVERSY

- Jan 2012: MMRC Contract: 126 aircraft, option 50%
- Fully assembled 18, balance to be manufactured by HAL (ToT)
- Lowest bidder based on life cycle costing
- HAL wanted Dassault to ensure quality of aircrafts
- Each aircraft cost Rs.746 crore
- 25th March 2015 CEO of Dassault “95% complete”
- April 2015: Modi – India to acquire 36 Rafale (FF)
- Tenders for 126 aircrafts cancelled (2015) and negotiation for 36 begins
- IGA signed in September (2016) for 36 aircrafts
- 50% offset clause (\$39B) back in India; 30% for DRDO
- \$2.9 billion (Rs.22000crore) for purchase of goods and services
- Reliance Group & DA creates JV (DRAL): Aero structure, electronics, engine companies and bolster R&D projects under (1 DDM) initiatives
- Escalation of cost from 715 crore – 1600 crore

ISSUES AND CONCERNS

- Charging the character of Contract (Buy & Make) to Buy
- Make-in-India a casualty
- IGA instead of Competitive tendering with all technically shortlisted firms of (2012) (like Typhoon (↓20%) price)
- Unsolicited offer – Rejected
- Qatar and Egypt paid Rs.1319 crore vs. Rs.1670 crore paid by India
- Inexperience of Reliance as IOP
- SC did not find material for commercial favouritism

MAJOR IRREGULARITIES IN CONTRACT

- Tailor-made specifications
- Resultant single tender: TEC/Field Trails
- Singh Tender
- Arbitrary exercise of repeat order and option clause
- Inspection reports
- Limited tendering
- L/D waiver
- Post contract management
- Phookan Commission

LETTER OF COMFORT: RAFALE

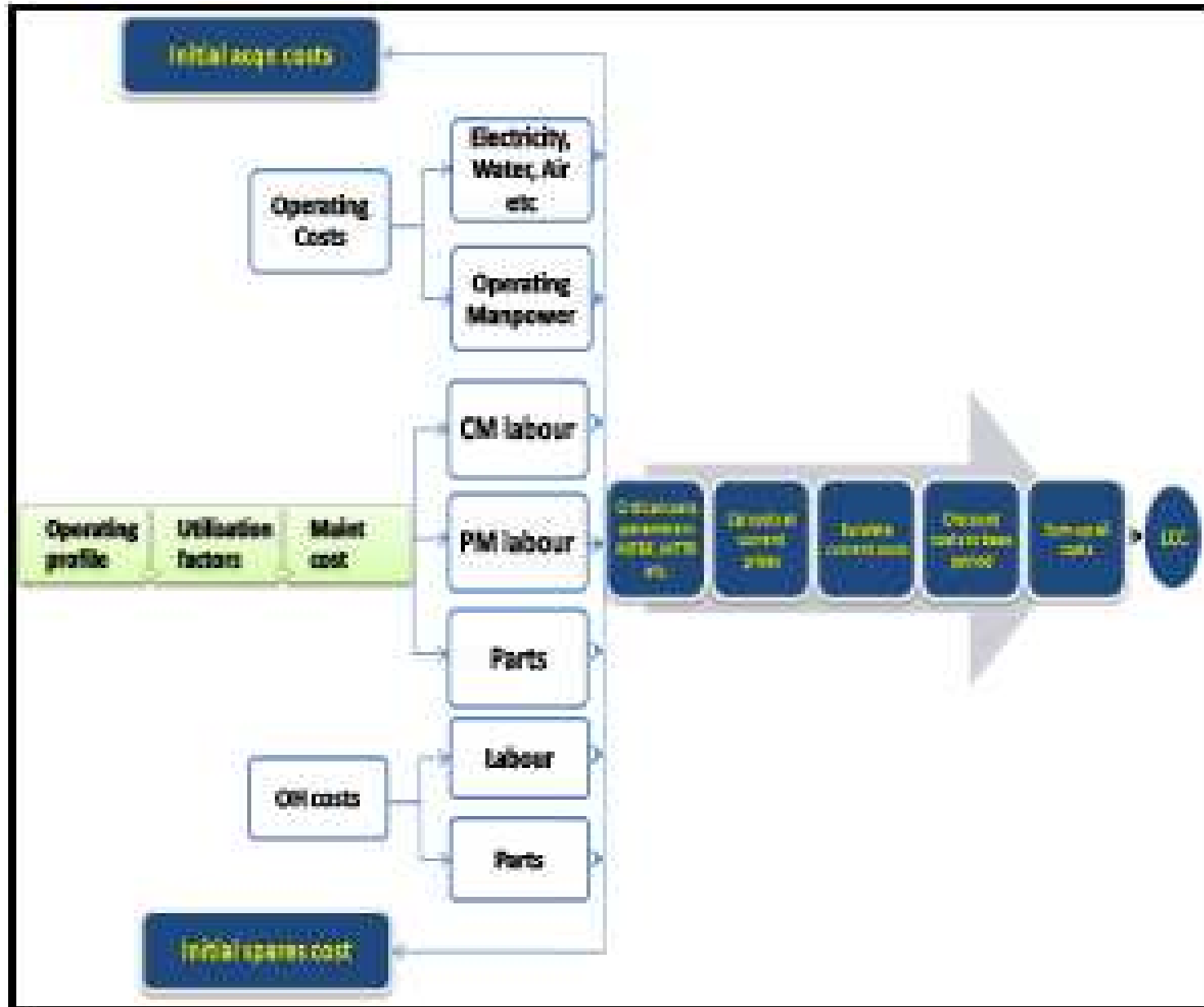
CONTRACTS

- Performance BGB given by foreign supplier
- Sovereign guarantee in case of Russia
- Foreign Military sales: USA
- Letter of Comfort: Parent corporation will provide its subsidiary with necessary resources to fulfil the contract
- EU Law: Does not require parent companies to fulfil obligations incurred by the subsidies
- Difficult to Enforce
- Intellectual Property Right: WTO (TRIPS)
- Many Decker: Ejection seat care

LIFE CYCLE COST

- Total Cost of Ownership of an asset over its life time, USA (60s), UK, Australia
- Cost of R& D, Testing, Production, Facilities, Maintenance, Environment Compliance& Disposal
- Acquisition Cost(28%), Operation Cost (12%), Logistics(60%)
- Total Discounted cost of Owning , Operating , Maintaining & disposing of the system
- Discount Rate, Escalation Rate
- Operational Availability of a System
- $A_o = \text{MTBM} / (\text{MTBM} + \text{DT})$, Where MTBM is Mean time between maintenance & DT is Downtime
- Applied in MMRC Contract : F-18E, F16N, Gripen, Mig 35 rejected after Flying Trials & TEC
- Rafael & Typhoon shortlisted for LCC, Rafael L1
- Heavy Lift Helicopter(Army), Multi Role Helicopter (Navy)

LIFE CYCLE COSTING PROCESS



SUPREME COURT JUDGEMENT

- KP Chowdhary vs. State of MP (1967): No implied contract between government and another person
- UOI and Hindustan Development Corporation (1996): One rate for big manufacturers and another for small manufactures.
- Held reasonable and not hit by Article 14.
- Decision making process to be reasonable, rational and not arbitrary and violative of Article 14
- Coal Block Allocation: Arbitrary
- Spectrum Allocation: Non Competitive

CORRUPTION IN THE DEFENCE SECTOR/OFFSET CONTRACTS

- Defence sector accounted for 50% of all bribery allegations (94-99)
- Capital Intensive outlays
- Opacity of Offsets
- Obsolete Technology Transferred
- Poor Job Creation Record: Keith Hartley
- No unambiguous economy wide net benefit (Brauer: 2004)
- Direct (40%), Indirect Military 35%, Civil indirect 25%: (European Union)

Source: Transparency International