Direct Transfer of Benefits: What Lies Ahead

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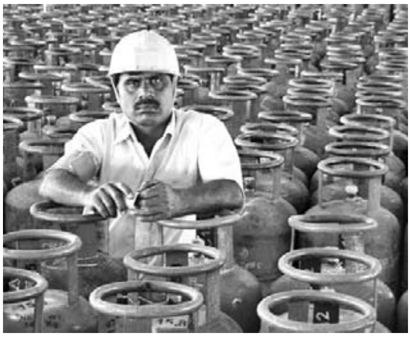

As long as implementation is adequate, the basic cash transfer project that has started, and the direct transfer of non-cash benefits based on Aadhaar-based authentication, are good ideas

INDIA'S WELFARE state has always committed significant resources to provide subsidies and services to the general public, and to certain identified segments of the population. Over the years, and especially as fiscal resources have grown rapidly in the previous two decades, the amount of money spent on welfare programs has reached staggering levels. As per our estimates, the Indian state's benefits transfers exceed Rs. 400,000 crores annually. But there have been concerns about the delivery of benefits to the intended beneficiaries. It is widely believed, and has been occasionally documented, that there are significant leakages in many of the schemes.

This January 1, the government started implementation of direct benefit transfer using Aadhaar numbers and bank accounts, for 20 government schemes. The project is being implemented in 20 districts, in what is planned to be the beginning of a staggered scale-up. Implementation has started with schemes that involve transfer of cash to beneficiaries. Schemes involving non-cash benefits, such as food, fertiliser, diesel and kerosene, are not yet proposed to be brought into the fold of this project. The Finance Minister said that there is no intention to bring those in the purview of this project.

This beginning is quite modest, given the government's usual approach of going with all guns blazing, scaling the initiatives nationally before reasonably testing them with small geographies and limited number of beneficiaries. I think this time it is the right approach, because an immediate scale-up could have led to very adverse consequences, not just for the beneficiaries but also for the idea of direct transfers.

Notwithstanding this modest beginning, there is considerable debate around this initiative, and its potential extensions. Looking at the debates around the recent initiative, it seems there are arguments around:

a) **The case for direct transfer of benefits:** Many people are arguing for or against this reform, because of

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the economic and social consequences of direct transfer of benefits.

b) **Challenges for direct transfer of benefits:** Some people accept the case for the reform, but warn about the challenges that may prevent a reasonable quality of design and implementation, and may in turn lead to consequences worse that the status quo.

In this article, I want to focus on both sets of issues. I want to use some empirical analysis as well as conceptual assessment of the issues to reflect on this and other similar reforms. But before I do that, let's differentiate between the various types of reforms that are possible under the catch-all phrase *direct benefit transfers*.

One needs to differentiate between three types of reforms that the government can undertake to get the benefits directly to the beneficiaries under various schemes:

a) **Direct delivery of cash benefits:** Reform of the existing cash transfer schemes to send the money through Aadhaar-enabled bank account. For example, instead of the school handing out the scholarships to students as cash, the student gets the money in her bank account. This kind of reform requires the beneficiaries to have easy-to-access bank accounts, and the scheme's management needs to align itself with the bank's transaction processing systems.

b) **Direct delivery of non-cash transfers:** Transfer of non-cash benefits using Aadhaar-based authentication. An example of this type of reform is requirement of Aadhaar authentication for getting a subsidised LPG cylinder. This reform requires development of Aadhaar-based authentication infrastructure at all outlets, and integration of back-end databases.

c) **Conversion of non-cash benefit to cash or cash-like transfer, and then delivering it directly:** An example could be the PDS system replacing the food and kerosene transfers to some form of voucher or cash. A reform such as this would involve strategic decisions about conversion of non-cash benefits to cash or cash-like forms, and developing systems for delivering the benefits. If the benefits are converted to cash, they could be processed through the banking system. There are also other possibilities, such as adding conditionality to transfer of benefits.

Any effort to convert non-cash benefits to cash or cash-like benefits entails complex reforms, and needs to be considered carefully and systematically. There are many variables to consider: who in the family will get the benefit; will there be conditionality attached; how will the conditionality be imposed; and so on. Each of these questions is important, and the government should carefully test the variations at small scale, before rolling out national scale reforms. This article does not go into the details of this type of reform. I only want to discuss the reforms that involve making the transfer of existing benefits direct.

One could reasonably consider that the two types of reforms that involve only making the transfer of existing benefits direct are relatively simple - both involve automation of the existing schemes, without substantial changes in the nature of the schemes. In this sense, these two are also similar reforms, but there are differences in the implementation challenges these types of reform face. The scheme essentially remains the same, but the delivery system is reformed, in different ways.

The government has started with automation of cash transfer. It may extend to the other types of reforms for some schemes but there is no proposal for that yet.

The case for direct transfer of benefits

For direct delivery of cash and non-cash benefits, the rationale is quite straightforward. It is claimed that in the delivery of benefits there are significant inefficiencies, some of which, such as the leakages due to duplicates and "ghost beneficiaries", can be addressed by automating the transfer process to ensure intended beneficiaries are directly authenticated before transfers are made. This directness of transfers is expected to not just directly improve the efficiency of the delivery systems, it will also empower the beneficiaries to demand their rightful benefits under various schemes, and hold the managers accountable. But this narrative is not enough. The costs of developing and maintaining Aadhaar are non-trivial, and so are the costs of integrating schemes with

Aadhaar-based delivery platforms. Proper analysis is required to make the case that the benefits outweigh the costs, at least in economic terms.

We at the National Institute of Public Finance and Policy (NIPFP) recently conducted a cost-benefit analysis of integration of Aadhaar programme with government schemes. The study looks at the extent to which reforms based on Aadhaar-enabled authentication can help reduce leakages from certain government schemes.

From the long list of government schemes, some lend themselves more easily than others to a reformed system of direct transfer of benefits, with the use of Aadhaar to authenticate beneficiaries. These include: Public Distribution System, Mahatma Gandhi National Rural Employment Guarantee Scheme (MNREGS), fertiliser subsidy, LPG subsidy, Indira Awas Yojana (IAY), payments to workers under the Integrated Child Development Services (ICDS), pension payments, cash and non-cash transfers in the education system, health programmes (payments to ASHA workers, payments under the Janani Suraksha Yojana). These schemes add up to about Rs. 2,10,000 crore of transfers annually (full sheet available at http://macrofinance.nipfp.org.in/releases/uid_cba.html). For all these schemes, it is assumed that there is just a basic automation of the delivery process using Aadhaar, and the scheme is not tinkered with.

For the PDS, the benefit accruing due to integration with Aadhaar is assumed to be in terms of reduction in leakages in the delivery of foodgrains (rice and wheat) and kerosene. For MNREGS, using the wage expenditure data and several social audit reports, the reduction in leakage in wage payments through muster automation and disbursement through Aadhaar-enabled bank accounts has been estimated. For fertilisers and LPG distribution, the diversion is estimated as a percentage of the government subsidy, which is assumed to be getting leaked or diverted for purposes beyond the subsidy's rationale. For other schemes, which include the Indira Awaas Yojana, Janani Suraksha Yojana, various pension schemes, scholarships, and payments made to workers under NRHM and ICDS, the leakages due to identfication errors are estimated as a percentage of the value of the transfer payment.

For many of these schemes, rigorously developed estimates of the actual level of leakages are not available. For PDS and MNREGS, some estimates of leakages are available, but even they are dated and not likely to be representative. So, the study assumes certain level of leakages by adjusting the leakage estimates from PDS and MNREGS downwards. In this sense, the study takes a conservative approach. Even after taking all costs into account, including the costs of Aadhaar development and maintenance as well as the cost of integrating Aadhaar with schemes, and making modest assumptions about leakages, of about 7-12 percent of the value of the transfer/subsidy, which are well below the estimates available for schemes, the study finds that the Aadhaar project would yield an internal rate of return of 52.85 percent to the government. The benefit is basically in the form of reduction in leakages, which are funds that the government can save and use for other purposes.

Even without going into the details of the study, given the magnitude of the transfers involved, even a moderately successful implementation should result in reduction in leakages that easily surpass the costs. For direct cash transfer, for example, banks seem willing to process the direct transfer of cash to beneficiaries for 3-4 percent of the transfer (the committee on direct cash transfers proposed 3.14 percent). In addition, there will be some expenses for integrating databases at the back-end, and developing and maintaining a process of ensuring that the list of rightful beneficiaries reaches the banks in a timely manner. So, if the reduction in leakages amounts is about 5 percent of the value of transfers, it makes economic sense to do direct transfers.

Based on this analysis, it can be argued that even modest assumptions about plugging the leakages lead us to conclude that direct benefit tranfers could lead to significant savings for the government. The other rationales for such direct transfers only add to the case.

Many benefits of such reforms are intangible and therefore difficult to quantify. For example, by making every individual identifiable, existing government welfare schemes can become more demand-led. Beneficiaries are better empowered to hold the government accountable for their rights and entitlements, thus influencing the way these schemes can be designed and implemented.

So, the economic and social case for direct delivery of benefits is reasonably strong, but this case rests on the assumption that a reasonably good implementation of reform is ensured. Let's look at the challenges to implementing the reforms.

Challenges for direct transfer of benefits:

There are certain common challenges for all the types of direct transfer reforms that the government can undertake, and then there are some challenges that are unique to each type of reform. Some of the key challenges are:

1) **Centre-State coordination:** Most of the schemes have the state governments playing the main role in implementing the scheme. To ensure there is adequate coordination between the reform plans and state-wise implementation is a significant challenge. The government approach of starting with a small scale, establishing the viability and benefits, and then going national, should help in making the case to the other states. This challenge also has a positive side. It is good that there is possibility for states to make changes to what the centre might propose. It is possible that some states may indeed do much better than what the centre may have planned. As we have seen in reforms of health, nutrition and education systems, some states may take lead in innovating, and the centre and other states can learn from their experiences.

2) **Partial coverage of Aadhaar:** Till date, Aadhaar numbers have been provided only to a quarter of the population. If there is any geography where these direct transfer reforms are implemented, but the Aadhaar enrolment is not universal, some beneficiaires could get temporarily excluded. This is a non-trivial problem, and the government ought to ensure that either there is universal coverage of Aadhaar wherever the reforms are implemented, or the old system of transfer is maintained parallely for some time, before it is clear that no beneficiary is going to be left out. Given the pace of Aadhaar enrolments, it should only be a matter of time before the coverage gets close to being universal.

3) **Inadequate development of the banking channel:** Wherever direct cash transfer is involved, the main role of delivering the transfers is played by the banking channel. There are a few challenges that may impede using the channel for transferring benefits:

a) Only about half of the population has bank accounts, and the coverage of the banking channel is far from adequate. Majority villages do not have conveniently located banking service points to transact. Reserve Bank of India (RBI) has done some reforms to ensure that since traditional bank branches are not viable in most rural areas, business correspondents of banks be made available universally. RBI has also pushed for opening zero-balance no-frills accounts or "basic savings accounts", which are special accounts for low value customers. Six years ago, RBI allowed for the business correspodent or the agenting model for banking. This is not long enough time to see full scale of this model. But, the trend is one of rapid scale-up of the business correspondent channel. In the two years from 2010 to 2012, the number of basic savings accounts grew from less than 5 crore to 10 crore, and the number of banking outlets grew from 54,258 to 1,47,534.

b) The rural banking channels have found it difficult to become viable, and the business correspondents need to be paid an optimal amount to make sure they process the benefits to the beneficiaries in a high quality manner.

c) There are infrastructure gaps that impede the development of banking networks in some remote geographies. Connectivity is poor, cash movement is risky, and it is difficult to ensure timely delivery of benefits. These gaps will be covered with time, but till then, these marginal areas must be given due consideration.

An important thing to realise is the interesting interplay between direct cash transfers and financial inclusion. If direct cash transfers come with reasonable compensation for the banking channel, they could catalyse rapid improvements in financial inclusion. The banking channels, especially in rural areas, could become more viable, and more people could enter the formal financial system. This also has other long term advantages for the welfare of beneficiaries.

4) **Challenges in automation of schemes:** Most schemes are presently run on archaic systems, and many do not have it in their DNA to maintain online databases and process the transactions electronically. This poses a considerable challenge of not just infrastructure development, but also of training and supporting the staffs. This challenge is particularly relevant for schemes where direct transfer of non-cash benefits is being attempted by automating the functioning of the scheme. For example, if PDS has to implement such reform, it would require not just development of a comprehensive database system to maintain the records, it would also require authentication infrastructure in all the PDS outlets, training those who run these shops, and providing ongoing technical support to them. This is a huge challenge in an existing system.

None of these challenges is insurmountable, but each requires careful consideration and coordination between policy and implementation. It is therefore a good idea to test these reforms at a small scale, fixing the difficult parts, and then taking them to scale.

To summarise, the case for direct transfer of benefits is quite strong, but there are also significant challenges in designing and implementing these reforms properly. If the challenges are not properly addressed, the reform has the risk of creating fresh problems for the schemes. As long as implementation is adequate, the basic cash transfer project that has started, and the direct transfer of non-cash benefits based on Aadhaar-based authentication, are good ideas, because they simply automate and improve the integrity of the process of the delivering the benefits, without altering the basic structure of the schemes. Converting the non-cash subsidies and services into cash or cash-like instruments requires more comprehensive evaluation, and has consequences that go beyond simple improvement in efficiency of delivery systems. ❑

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