

Policy Brief # 11

Optimising Commissions and Payout Mechanism For G2P Payments Under Electronic and Direct Benefit Transfer

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A variety of government ministries and departments, both at the centre and in the states, have distributed cash benefits to the poor and underprivileged under a range of welfare schemes for over six years. As the business correspondent (BC) model achieved critical mass in terms of customer service points (CSPs or agents), progressive governments (such as Andhra Pradesh) took advantage of the better outreach and greater security they afforded to channel cash benefits. These governments accelerated the disbursement of benefits through the BC channel, authenticated by fingerprint biometrics. Subsequently UIDAI's *Aadhaar* allowed the opportunity for a more secure, nationally de-duplicated, centralised and lower cost mechanism for fingerprint authentication and electronic KYC (e-KYC). Direct benefit transfer (DBT)¹ with *Aadhaar* authentication was launched by the government from 1st January 2013 and has thereafter been extended to [28 identified schemes in 121 districts](#).²

Despite government agencies and Unique Identification Authority of India (UIDAI) being upbeat about direct cash transfers, a major barrier EBT³ and DBT programmes have encountered is the unwillingness of banks to scale up G2P payments through business correspondents.⁴ The major underlying reason is inadequate compensation to (beneficiary)⁵ banks for managing G2P payments. State governments have adopted diverse policies for compensating banks. A [task force](#) constituted of the Reserve Bank of India (RBI), UIDAI, NIC,⁶ IBA,⁷ NPCI,⁸ Controller General of Accounts, Ministries of - Rural Development; Food and Public Distribution; Petroleum and Natural Gas; and Departments of - Financial Services, Expenditure, Fertilizers; under the chairmanship of Nandan Nilekani, Chairman UIDAI, recommended a last-mile transaction processing fee of 3.14%. However the implementation of these recommendations has been resisted, with no government agency implementing them yet. The appropriate consideration for disbursement of G2P payments remains a widely debated question.

The second big question that has not found an empirical and rational solution is the mechanism for the distribution of pay-outs further down the chain to the business correspondent network managers (BCNMs) and their CSPs; and the variants, if any, according to factors such as rural or urban area, type of terrain (i.e. hilly, unconnected) or demographics (i.e. deeply tribal) and so on.

This Policy Brief provides potential solutions to these two questions. Most of the data and analysis is derived from *MicroSave's* experience and lessons learned based on extensive research and studies in India, covering banks, BCNMs and CSPs, as well as consumers and non-consumers of financial services.

¹ G2P payments carried out through National Electronic Fund Transfer (NEFT) and non *Aadhaar* Payment Bridge (APB) transactions using Central Plan Scheme Monitoring System (CPSMS) are also included in DBT.

² <http://planningcommission.nic.in>

³ Electronic Benefit Transfer

⁴ See *MicroSave* Policy Brief 9: [Improving the Reach and Quality of Agent Networks in India](#)

⁵ Sponsor banks are treasurers to the government and earn from the float of the G2P funds. Beneficiary banks are responsible for disbursement of payments to the end beneficiaries and are the ones who find the compensation inadequate.

⁶ National Informatics Centre

⁷ Indian Banks' Association

⁸ National Payments Corporation of India

A summary of recommendations

1. A vast majority of the CSPs disbursing G2P payments receive compensation that is far lower than the minimum wages prescribed by the respective state governments. Ironically it is the same minimum wage that many of these CSPs are distributing to others. The minimum compensation to the CSPs (at least equivalent to the minimum wage prescribed in the state) has to be mandated through policy. The model for determining CSP compensation cannot be based purely on the volume of cash disbursed, as it is influenced by many factors outside the control of CSPs. It needs to be based on a prescribed fixed minimum monthly amount, with the rest (about 25%) linked to the cash disbursed. Correlated to the minimum wages defined by the various governments, for states like Bihar, Uttar Pradesh, Orissa, Rajasthan and Madhya Pradesh the fixed monthly compensation should be Rs. 2,100 per CSP; and for states like Andhra Pradesh, Maharashtra and Karnataka it should be Rs. 2,400 per CSP. The rest of the payout should be variable - at about 0.3% percent of the cash disbursed. While a few BC institutions⁹ are following variants of this model voluntarily, it needs to be mandated in the form of policy guidelines to make it universal.
2. In order to ensure transparency and efficiency of the payout, CSPs should be paid electronically - directly into their accounts by the parent bank. A policy intervention is required to make it mandatory for the banks to ensure accounts are opened at any convenient bank (including Regional Rural Banks (RRBs) or Cooperative Banks that have upgraded to core banking) for all the CSPs involved with G2P disbursements, and their dues are credited directly on a monthly basis.
3. Most institutional BCNMs are in a position to achieve a reasonable gross margin from G2P payment disbursement. However, currently this is being achieved at the cost of the CSPs, who are receiving a much lower compensation than desirable. For BC institutions to continue to be viable (defined as a net profit¹⁰ in single digits or sub 10%), their compensation should be 0.6% to 0.7% of the cash disbursed. This excludes the compensation to CSPs, which, as recommended above (fixed minimum, with a variable payout in the range of 0.3%), needs to be paid to them directly by banks, instead of being routed through institutional BCs.
4. Most banks are currently losing money servicing G2P payment disbursements. While they receive 1.0% to 2.0% (in a best case scenario) of the cash disbursed, their total 'cost to disburse', including BC and CSP costs are in the range of 3.0% or more. As a result they are making a loss for every rupee disbursed. This does not make business sense. In order for banks to make a reasonable income, the payout to banks should be in the range of 3.0% to 3.3%¹¹ (of this 1.9% should be passed on to the BCs and the CSPs; while 1.1% can be retained by banks to cover their costs and realise a small margin).
5. 3.0% payout to banks is often viewed by the governments as an unacceptable financial burden, but this is short-sighted. Our findings¹² corroborate other similar ones,¹³ that governments' savings can significantly exceed 4.0%¹⁴ of the welfare payments disbursed, by making the delivery of G2P payments efficient¹⁵ through *Aadhaar* enabled DBT. Fundamental to this would be to ensure a business case for banks and sustainability of BCs and CSPs – the last mile service providers.

⁹ Individual BCs of [Bank of India](#) receive a fixed monthly compensation of Rs 3,500 per month in rural areas, for an initial period of up to six months, any income over this, generated by the CSPs, is based on a variable model; [Manipal Business Solutions](#) provides a fixed compensation to urban CSPs (through its BC) for about 15 days of work per month.

¹⁰ See details and computation of gross margin and net profit below.

¹¹ This is nearly the same compensation as the task force headed by Nandan Nilekani had recommended.

¹² Refer [MicroSave Case Studies on DBT](#)

¹³ A cost-benefit analysis of *Aadhaar*, NIPFP, 2012

¹⁴ See box ahead. Net of the 3.0%, this means governments can still potentially realise a savings of 1% or more of the cash subsidy budget

¹⁵ Through elimination of ghost beneficiaries and other forms of leakages; reduction of cash in the system; enhanced efficiency of reconciliation; and savings through disintermediation.

6. However, if the governments decide to limit the payout to 2.0%, due to budgetary constraints, the distribution across banks, BC institutions and CSPs should be as follows. A relative comparison for the case of 3.0% is also given.

| Payout % | 2.0% | 3.0% |
|------------|------|------|
| Bank share | 0.2% | 1.1% |
| BC share | 0.6% | 0.7% |
| CSP share | 1.2% | 1.2% |

The rationale and analysis underlying each of these recommendations is given below.

What should be the CSPs paid?

Starting at the very last-mile of delivery of payments, let us assess what is an equitable compensation to the CSPs/agents disbursing G2P payments. For a dedicated CSP with earnings from disbursing EBT/DBT payments as the sole income stream, the following table illustrates the feasible quantum of cash disbursement and the potential for earnings.

| Metrics for an average CSP ¹⁶ | Unit | Typical Range | Average |
|---|---------------|-------------------|---------|
| Average transactions in a day | # | 30 to 90 | 40 |
| Transaction ticket size (disbursement value) | Rs. | 150 to 250 | 200 |
| Working days available | # | 15 to 24 | 18 |
| Volume of cash distributed per month | Rs. | 70,000 to 500,000 | 200,000 |
| Income expectation per minimum wage policy ¹⁷ | Rs. per month | 2,000 to 3,500 | 3,000 |
| Payout percent to meet minimum wage expectation (for a full variable fee model) | % | 0.7% to 3.0% | 1.5% |

This analysis excludes time required by CSPs for cash (liquidity) management and end of day, and end of cycle reconciliation of books. Accounting for these activities, the actual time left for disbursements is lower. Accordingly the potential for cash disbursement and earnings is revised below.

| Metrics for an average CSP | Unit | Typical Range | Average |
|---|---------------|-------------------|---------|
| Average transactions in a day | # | 30 to 90 | 40 |
| Transaction ticket size | Rs. | 150 to 250 | 200 |
| Working days available | # | 12 to 20 | 14 |
| Volume of cash distributed per month | Rs. | 50,000 to 450,000 | 180,000 |
| Income expectation per minimum wage policy | Rs. per month | 2,000 to 3,500 | 3,000 |
| Payout percent to meet minimum wage expectation (for a full variable fee model) | % | 0.8% to 4.0% | 1.7% |

¹⁶ Most metrics are computed using data from *MicroSave's* research for MGNREGA and pension payment disbursements under NSAP as these constitute the flagship G2P payment schemes. The disbursements under MGNREGA for FY 2012-13 were [Rs. 271.3 billion](#), compared to [Rs. 4.0 billion](#) under 28 other schemes through DBT in CY 2013.

¹⁷ [The minimum wage guaranteed by most states under MGNREGA is between Rs 140 and Rs. 174 per day of work](#). The CSPs disbursing MGNREGA, pensions and other government payments, should be expected to earn at least the minimum wage, if not more.

In contrast to this, our experience, analysing the earnings of a range of CSPs, exhibits the following trend in their income streams.

All figures in Rs.

| | CSP 1 | CSP 2 | CSP 3 | CSP 4 | CSP 5 | CSP 6 | CSP 7 | CSP 8 | CSP 9 | CSP 10 |
|--------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|--------|
| Gross Income/Month | 2,882 | 2,910 | 1,169 | 885 | 3,035 | 1,439 | 1,648 | 5,730 | 3,500 | 1,561 |
| Enrolment Income | - | - | - | - | - | - | - | 3980 | 3000 | 550 |
| Transaction Income | 2,319 | 2,347 | 606 | 322 | 2,472 | 876 | 1,085 | 1750 | 500 | 1010.5 |
| Fixed Salary | 563 | 563 | 563 | 563 | 563 | 563 | 563 | | | |
| Expenditure/Month | 572 | 672 | 572 | 622 | 672 | 672 | 100 | 300 | 250 | 150 |
| Mobile | 100 | 200 | 100 | 100 | 100 | 100 | 100 | 200 | 100 | 50 |
| Travel | 100 | 100 | 100 | 150 | 200 | 200 | 0 | 100 | 150 | 100 |
| Other expenses | 372 | 372 | 372 | 372 | 372 | 372 | 372 | - | - | - |
| Net Income/Month | 2,310 | 2,238 | 597 | 263 | 2,363 | 767 | 1,548 | 5,430 | 3,250 | 1,411 |

This demonstrates that a significant proportion of the CSPs, amongst those dependent on G2P payment disbursements as a full time livelihood, are earning less than 25% of the prevailing minimum wage.

The first key take-away for optimising the G2P payment delivery is to ensure that CSPs receive an income that sustains their interest in the business and is at the very least is comparable to the minimum wage. If the percentage based payout model were to be extended to them, there would be considerable dependence on the number of transactions and the transaction ticket size, both of which vary significantly by region, seasonality, local migration and so forth. It is therefore appropriate that a large part of the income (say 70% to 80% of the minimum wage prescribed by the respective state government) is received by the CSPs as a fixed monthly payout. Using the minimum wage rate¹⁸ for the states that have the highest number of CSPs, this comes to Rs. 2,100 per CSP per month, for states like Bihar, Uttar Pradesh, Orissa, Rajasthan and Madhya Pradesh and Rs. 2,400 for states like Andhra Pradesh, Maharashtra and Karnataka. The rest of the payout, to match the minimum wage, can be variable, and equivalent to about 0.3% percent of the cash disbursed.

The second take-away is around an optimal mechanism for delivering the payout to CSPs. [MicroSave studies and surveys](#) have frequently demonstrated that even where banks are paying the BC institutions adequately for managing G2P payment disbursements, the last-mile CSPs are not suitably compensated; and whatever is paid is often delayed by several months. There has to be a mechanism to ensure that CSPs directly receive their dues in full and on time. This can be achieved by banks adopting the practice of having mandatory accounts for CSPs at any bank nearest/convenient to them; and by directly crediting their dues (as per the model outlined earlier) to these accounts on a monthly basis (exactly the way wages and salaries are paid electronically directly into recipient accounts). This would serve three objectives for the CSPs – (a) ensure CSPs receive their entitlement in full; (b) ensure their dues are received on time; and (c) reduce the burden of cash management and increase available time/efficiency for disbursements. This third advantage would be possible as the same (or a similar) bank accounts should also be used by banks or BC institutions to transfer cash to be disbursed, instead of continuing the practice of using gunny bags to safe-keep piles of cash and transit long distances. A common practice currently followed that involves high risk, and is both inconvenient and inefficient.

What should be the BC institutions paid?

If these practices for CSPs are accepted and implemented, the next question is - what is an appropriate compensation to the BC institutions, when they manage the last mile delivery of G2P payment disbursements for banks?

Analysing four different BC institutional models which between them cover diversities of – rural/urban topography, scale of operations (national/regional/local), technology (POS, micro-ATMs and mobile), cash management (cash-light/cash-heavy), commission model (fixed, variable, blended), operating and reconciliation process variants and so on, the results are as under.

¹⁸ [State wise rates for FY 2012-13](#) extrapolated for FY 2013-14 using the Consumer Price Index related to Agricultural Labourers (CPIAL), to achieve a real rate of Rs. 100 per day with year 2009 as the base, per the guiding principles of the MGREGA policy.

| Institutional BC Financials | BC 1 | BC 2 | BC 3 | BC 4 |
|--|-------|-------|-------|------|
| Revenue per disbursement (Rs.) | 4.81 | 10.95 | 4.67 | 3.95 |
| <i>Enrolment Income</i> | 0.50 | 0.02 | 0.33 | 0.28 |
| <i>Transaction Income</i> | 4.31 | 10.92 | 4.34 | 3.67 |
| Cost per disbursement (Rs.) | 3.48 | 8.00 | 3.74 | 3.57 |
| <i>Direct cost</i> | 3.00 | 6.15 | 3.23 | 2.97 |
| <i>Platform / tech cost</i> | 0.17 | 0.35 | 0.18 | 0.29 |
| <i>Management and supervisory cost</i> | 0.31 | 1.50 | 0.33 | 0.31 |
| Net earnings per disbursement (Rs.) | 1.33 | 2.95 | 0.93 | 0.38 |
| Percentage margin for institutional BC | 27.6% | 26.9% | 20.0% | 9.5% |
| Average disbursement ticket size (Rs.) | 248 | 155 | 249 | 237 |
| Gross BC revenue as % of disbursed value | 1.9% | 7.1% | 1.9% | 1.7% |

This is the current situation where BC institutions realise a high gross margin by avoiding paying appropriate compensation to CSPs. If this were modified to reduce the revenue expectation for the gross margins to 15% while raising the compensation for CSPs to the equivalent of minimum wage prescribed, the outcome would be as follows.

| Institutional BC Financials | BC 1 | BC 2 | BC 3 | BC 4 |
|--|-------|-------|-------|-------|
| Revenue per disbursement (Rs.) | 6.56 | 11.33 | 7.47 | 6.58 |
| Cost per disbursement (Rs.) | 5.57 | 9.63 | 6.35 | 5.59 |
| <i>Direct cost</i> | 5.09 | 7.78 | 5.84 | 4.99 |
| <i>Platform / tech cost</i> | 0.17 | 0.35 | 0.18 | 0.29 |
| <i>Management and supervisory cost</i> | 0.31 | 1.50 | 0.33 | 0.31 |
| Net earnings per disbursement (Rs.) | 0.99 | 1.70 | 1.12 | 0.99 |
| Percentage margin for institutional BC | 15.0% | 15.0% | 15.0% | 15.0% |
| Average disbursement ticket size (Rs.) | 248 | 155 | 249 | 237 |
| Gross BC revenue as % of disbursed value | 0.6% | 2.3% | 0.7% | 0.7% |

There are two key insights from this analysis:

1. Nearly all institutional BCs are making good gross margins (at the EBIDTA level),¹⁹ ranging from 9.5% to as high as 27.6%.
2. For a reasonable gross margin of 15% for the institutional BCs, the gross revenue as a percentage of the disbursed cash needs to be in the range of 0.6% to 0.7% (excluding the payout to CSPs at a minimum threshold level, as described above and paid directly by banks). At this level the BC institutions are likely to be reasonably sustainable, considered as a net profit (PAT)²⁰ in the range of 10%.

What compensation should the banks receive?

Finally we analyse how much the banks should receive in order to adequately compensate both the BC institutions and the CSPs, while retaining a small profit themselves, if they are expected to participate in G2P payment distribution as a business and not as a CSR²¹ activity.

A review of the earnings and the costs of two large banks, involved with G2P payment disbursement at scale, highlight the following.

¹⁹ Earnings before interest, depreciation, tax and amortisation (EBIDTA)

²⁰ Profit after tax (PAT)

²¹ Corporate Social Responsibility

| Bank Financials | Bank 1 | Bank 2 |
|---|--------|--------|
| Revenue per rupee of cash disbursed (%) | 2.26 | 2.26 |
| Income from disbursals (%) | 2.00 | 2.00 |
| Float income (%) | 0.26 | 0.26 |
| Cost per rupee disbursed (%) | 3.19 | 2.92 |
| Bank costs (%) | 0.96 | 0.98 |
| BC (including CSP) payout (%) | 2.23 | 1.94 |
| Gain (Loss) per rupee disbursed (%) | -0.93 | -0.66 |
| Gross margin for the bank | -41.2% | -29.2% |

In order for the banks to achieve a reasonable gross margin (EBIDTA) of 10.0%, the amount required to be paid to banks is determined as under.

| Bank Financials | Bank 1 | Bank 2 |
|---|-------------|-------------|
| Revenue per rupee of cash disbursed (%) | 3.55 | 3.25 |
| Income from disbursals (%) | 3.29 | 2.99 |
| Float income (%) | 0.26 | 0.26 |
| Cost per rupee disbursed (%) | 3.19 | 2.92 |
| Bank costs (%) | 0.96 | 0.98 |
| BC (including CSP) payout (%) | 2.23 | 1.94 |
| Gain (Loss) per rupee disbursed (%) | 0.36 | 0.33 |
| Gross margin for the bank | 10.0% | 10.0% |

The key insights are:

1. Leading banks are currently losing money while servicing G2P payment disbursements. While they receive about 2.0% (that too in the best case scenario in Andhra Pradesh, in most other states it is a much lower payout of 1.0% or even lower), and earn another 0.26% on the float, their total cost to disburse, including the compensation to the BCs and the CSP, is in the range of 3.0% or more. As a result they are making a loss for every rupee disbursed and this is not viable in the long term. The more they disburse the more they lose – hence banks' resistance to rolling out BCs at scale.
2. In order for banks to make a reasonable gross margin of 10.0%²², the payout to banks needs to be in the range of 3.0% to 3.3%.
3. The payout would need to be an even higher percentage of 3.5%, if the considerations of minimum wage payout to CSPs and terrain (hilly, remote or tribal regions) related constrains were to be included.

²² Considered lower than the 15.0% for the BC institutions, as for the banks, this is one of their businesses and there is a possibility of keeping margin expectations lower than other businesses and achieving higher blended margins. The same is not true for BC institutions as they have a smaller scale and this is their primary business, hence margin expectations are higher.

²⁰ *ibid*;

²¹ *ibid*; *MicroSave* research on DBT models in Andhra Pradesh.

Why the 3.14% payout recommended by the task force headed by Nandan Nilekani is a win-win proposition for everyone?

According to estimates,²⁰ the effective throughput of various welfare schemes ranges from 60% to 85%. About 6.0% of the budget is earmarked for administration of the schemes, while 10% to 35% of the funds assigned are lost in delivery. These inefficiencies, and direct and indirect losses are on account of ghost and duplicate beneficiaries; fake and inflated muster rolls; cost of cash management; accounting and reconciliation; and cost of multiple intermediaries involved in disbursement. It is estimated²¹ that 8% to 10% of the losses are due to fake and ghost beneficiaries. With *Aadhaar* based Direct Benefit Transfer, along with optimisation of cash management (achieved by directing funds to CSP accounts instead of paying in cash, as explained earlier, and other such measures), these losses can be brought down significantly. Assuming a realistic 50% improvement, this can translate to a saving of 4.0% to 5.0% of the budget.

On an average, the current payout to banks by various state and central government ministries ranges from 1.0% to 2.0%. If it were raised to 3.0%, in order to realise the benefits outlined above, the additional cost to the governments would be 1.0% to 2.0%. Considering the anticipated savings above, there would still be a net gain of 2.0% to 3.0% for the governments.

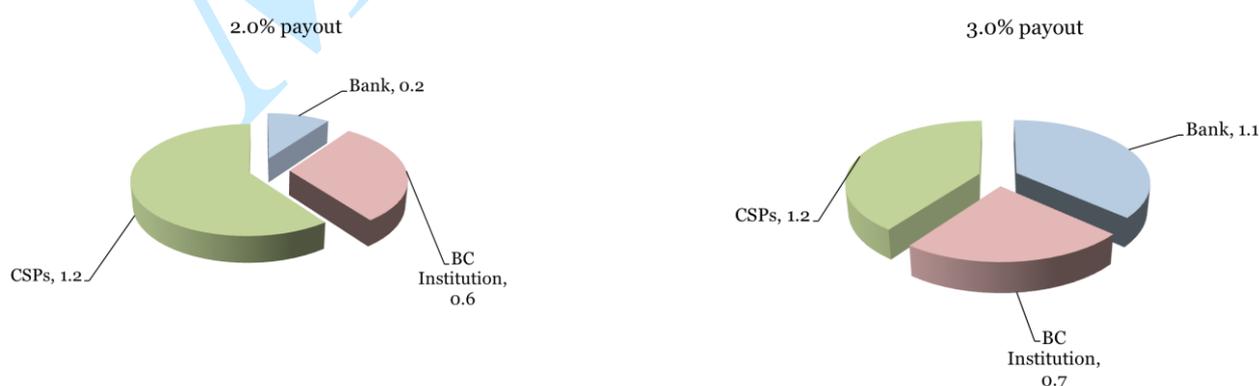
In view of this if the recommendations of 3.14% payout by the task force led by Nandan Nilekani are implemented, it can be a win-win outcome for banks, BCs, CSPs, the governments and of course the beneficiaries (who would have the opportunity to receive their dues *in full* and more conveniently through a CSP in their neighbourhood). As the average transaction ticket size is Rs. 200, the proposed cap of Rs.20 per transaction on the fee also ensures that low value transactions are not penalised.

What should be an equitable payout distribution model, if the total compensation has to be limited to 2.0% due to government's budgetary or other constraints?

In the case that the total compensation has to be limited to 2.0% due to budgetary or other constraints, as is being currently debated, the following can be an equitable method of distribution.

- Payout to CSPs: Basis the analysis of a minimum wage equivalent payout to the CSPs, it translates to about 1.2% of the cash disbursed by the CSPs.
- The remaining 0.8% should be distributed as 0.6% to the BC institution and 0.2% retained by the bank (apart from the small earnings from the float). We believe this would tantamount to about 10% net margin (PAT) for the BC institutions, while the bank would continue to lose. It is clearly not a case of sustainability, but can be the most optimal distribution possible, under the constraints.

Potential optimal distribution across banks, BCs and CSPs, with a 2.0% and a 3.0% payout is exhibited below.



In summary, unless the banks, BCs and CSPs are adequately compensated for their very critical role in supporting the last mile delivery of G2P payments, the quality of service to the beneficiaries would continue to be compromised and the objectives (of transparency, effectiveness, efficiency, convenience and so on), underlying direct transfer of benefits cannot be realised.