

Redesigning India's **Social Protection** **Financing Architecture** to meet the Challenge of COVID-19

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States are at the frontlines in the battle against COVID-19. The key areas which need significant short and medium term interventions – health, agriculture and social protection – are State subjects. However, States are stymied by the lack of resources. In the last few weeks, several options for increasing finances to the States have been tabled. These include, loosening fiscal responsibility limits on States, increasing ways and means advances, including making available a special zero interest window for a fixed period, a special COVID-19 grant window, as well as, speeding up and increasing central transfers for existing schemes.

The last route has not received adequate attention in the current debate on Centrally Sponsored Schemes (CSS) and Central Sector Schemes (CS)². These sources of financing are critical because they are the primary means through which States spend in two key areas of expenditure relevant to dealing with the COVID-19 crisis – health and social protection. In health expenditure for instance, a significant proportion of non salary expenditure (upto 80% in some States) is financed through the National Health Mission (NHM). Similarly key programs for social protection – like the Mahatma Gandhi National Rural Employment Guarantee Scheme (MGNREGS), Mid-Day Meals, Integrated Child Development Services (ICDS), to name a few are financed through this window.

There are two challenges with this current mode of financing. **First**, for most CSSs, States have to contribute a significant (up to 50% for supplementary nutrition under ICDS and 40% for NHM) share of funds for the scheme from their own budgets. This puts a strain on State budgets. **Second**, this scheme based model of financing functions on the principles of a centrally designed, one-size fit all model, which even in ordinary times, results in administrative fragmentation (there are over 600 CS schemes alone) and undermines State flexibility. Fragmentation is also an impediment to designing a portable social protection mechanism for migrant workers as multiple schemes are mapped to multiple ministries with different fund flow and targeting requirements.

Further, this centralised and fragmented financing does not accommodate for the specific challenge that COVID-19 presents. COVID-19 outbreaks will be localised within States, placing differential financial needs linked to state-specific health capacities and socio-economic profiles.

Moreover, the economic impact of periodic lockdowns (even in a graded lockdown approach) will place differing financial constraints on States. Responding to COVID-19 thus requires a differentiated but co-ordinated response to all aspects of the crisis from health to social protection, akin to a pooled financial system.

The financing challenges described here are not limited to CSS and CS. The current design of grant funding being used for additional disaster support to States – the National Disaster Risk Management Fund (NDRMF) and State Disaster Risk Management Fund (SDRMF), too is not designed to respond to the COVID-19 crisis. According to Government of India (GoI) notifications, these funds are to be used for States' specific needs related to health and relief measures needed. However, here too the fund sharing ratio, as per recommendations of the 15th Finance Commission interim report, place a financial burden on States (current ratio for SDRMF is 75:25³). Moreover, the current inter-state distribution formula is fixed and does not account for the state-specific health and financial needs that the unique nature of the COVID-19 crisis presents. Given the demands of COVID-19, an appropriate financing formula will have to be dynamic and responsive.

Against this backdrop, it is critical to re-consider the design of the current inter-governmental fiscal transfer system for responding to the health and social protection needs of COVID-19. We propose a reformed architecture, based on the principles of decentralisation, consolidation, and convergence. The institutional foundations of this reformed fiscal structure will lie in the creation of a new emergency council (akin to the GST council), within the fold of the Inter-State Council.

Redesigning the inter-governmental fiscal transfer system for COVID-19 response

1. NEED COUNCIL

The nature of the COVID-19 crisis requires a differentiated but co-ordinated response to all aspects of the crisis from health to social protection. India is currently only in the early days of the COVID-19 crisis. In the next 2-3 months, the current emergency response will need to be institutionalised in to a dynamic, decentralised structure that is able to provide financing and capacity support customised to the nature of the disease and state-specific

needs. Decentralised co-ordination of this nature requires an institutional platform.

We thus propose the establishment of a National Empowered Emergency Disaster Council (NEED Council). Unlike the GST Council, this is envisaged as a political body of Chief Ministers, the Prime Minister and senior central ministers. The composition is similar to that of the Inter-state Council (ISC). One can conceive of a mechanism where the ISC functions as the NEED Council, in the same manner as the Election Commission of India takes over the administration, during an election.⁴

The NEED Council should be supported by the National Disaster Management Authority and a COVID-19 specific, NEED funding window should be created through the NDRMF (the NDRMF could be temporarily redesigned for COVID-19). The NEED Fund should include three elements:

- a. A base fund (fixed % of GDP) that is immediately accessible to both Centre and States (this should include NDRMF allocations)
- b. Funds received from repurposed CSS expenditure (see part 2 below for details). The extent of repurposing can be in tranches, based on the severity of the crisis. The Centers' current relief package, which is being implemented through individual CSS should be subsumed into this structure.
- c. New funds made available through deficit financing, new tax revenue (e.g., increased excise on petroleum), international institution loans, e.g. from multilateral financial institutions

Specifically, for social protection related programs, we propose a technical sub-group that will be constituted under the NEED council. This group will be responsible for arriving at a consensus on a broad basket of core social protection schemes, agree upon fiscal transfer formula, devise a coordination mechanism for handling payments linked to inter-state migrants⁵ (this would include reconciling invoices raised by destination states to the states of domicile) and sharing best practices.

The NEED council will also be the primary body for monitoring and reporting on expenditure. The council will periodically prepare reports on spending plans and

outcomes achieved and table these reports to Parliament and in the public domain. In the first phase (the first three months) funds could be distributed to states based on population with additional weightage for health capacity, linked to the NITI Aayog's health and nutrition indices. Once the functioning of the council has been established, the formulae must be revisited, linked to the nature of the COVID-19 outbreaks and specific economic hardships being experienced in States.

2. REPURPOSING CSS AND CS

Against the backdrop of the COVID-19 crisis, the focus needs to be on three key areas of grant support to States: **Health**, both to deal with the immediate crisis, as well as, to ensure non-COVID-19 related health shocks do not occur (we are already seeing a famished Tuberculosis campaign); **Food** to provide basic food security for vulnerable populations, and **Cash**, for everything else.

The current approach adopted by GoI for financing relief measures is through the Pradhan Mantri Garib Kalyan Yojana (PMGKY) which essentially seeks to top up financing through the existing CS and CSS route. Health expenditure too is primarily being incurred through the National Health Mission. However, this scheme-based approach is inadequate. An alternative approach is to support States by buttressing their efforts through an untied grant window in the NEED council.

This can be achieved by bundling together the CSS and CS into an untied grant fund for States to draw from, without being constrained by central guidelines and line-item budgeting. CSS and CS for non core COVID-19 activities (excluding health and social protection) have currently been required to scale down spending to 15% for the first two financial quarters of FY 2020-21. The funds from these schemes should be bundled into the COVID-19 grant. In addition, **the fund sharing ratio, at least for six months, in core schemes for health and nutrition should be suspended and states should receive 100% funding from the Center.** The State share could be redesigned as a long term zero interest loan from the Centre to States, to be repaid in FY 2021-22 (or when the crisis abates).

Pooled central scheme funds can be re-allocated to three specific thematic grant windows:

- a. Health:** Current NHM budget (Rs. 34,115 crore⁶) can be supplemented by temporary expenditure switching from infrastructure-related CSS such as Pradhan Mantri Awas Yojana (PMAY), Swachh Bharat Mission (SBM), Jal Jeevan Mission (JJM) and Pradhan Mantri Gram Sadak Yojana (PMGSY). All non-salary funds from these programs for the first two financial quarters of the current financial year, should be additionally allocated to ensure adequate health infrastructure in states, including for upgrading health and wellness centres and Primary Health Centres (PHCs) to operate as fever clinics. In its latest advisory on cash flow management, the Ministry of Finance (MoF) has already mandated significant reduction of planned expenditure for the first two quarters of FY 20-21. These funds should be repurposed to NHM or the recently announced Emergency Response and Health Systems Preparedness Package.
- b. Food Security and Livelihoods:** The PMGKY has enhanced entitlements under the Public Distribution System (PDS), free gas connections and committed to paying pending wages under MGNREGS. However, the critical input to food security is coming from State governments, many of whom have set up community kitchens for migrant workers, expanded mid-day meal schemes and other state-specific feeding programs. These need additional funds. To provide these funds, the PMGKY should merge all targeted food and dry ration related schemes (Mid Day Meals, supplementary nutrition component of ICDS) into a single food security window that States can draw from to supplement their own food-related initiatives. This will be in addition to enhanced provisions made through PDS. To cater to returned migrant populations the PDS must abandon the current targeted approach and function as a demand-based system i.e. any rural/urban resident in need of grains, pulses and other entitlements coming to the PDS store should be eligible. If ID requirements are deemed necessary, then the PDS should be linked to any universal ID - the voter card, Aayushman Bharat card, or Aadhaar card could be used in the absence of a ration card.
- c. Cash for Social Protection:** Rather than the current fragmented approach of the PMGKY (providing Rs. 500 in Jan Dhan Accounts), funds currently allocated across scholarships, pensions, maternity benefit and wage payments under MGNREGS (for places where work sites aren't open – either because of difficulties in opening sites with social distancing or in places where districts are declared hotspots) should be pooled into one single bucket to ensure additional cash directly to beneficiaries (to all JDY and MGNREGS bank account holders or alternatively go universal in spatial targeted poor areas). Where JDY accounts are being used (i.e. not dormant), funds should be delivered directly into JDY accounts. In places where the bank to household distance is high and accounts dormant, States can determine means of directly providing cash to people through Panchayats or banking correspondent networks. Back of the envelope calculations for CSSs aimed at maternity entitlements, pensions and scholarships (not including MGNREGS) indicate that this would be just over Rs. 18,500 crore in FY 2020-21 BE.
- Until such time as schools are closed, additional resources could also be mobilised from the education sector. While it's imperative that teacher salaries get paid, on average, salaries under Samagra Shiksha accounted for only 37% of the Samagra Shiksha Budget leaving a significant non-wage component that can be deployed for social protection funds.
- In the long term, a concrete national social protection strategy will need to be developed. This will help identify core programs applicable nationally (e.g. MGNREGS, PDS, social insurance for migrant workers etc.), designed with flexibility for States to deploy funds as appropriate to their specific conditions. In addition to core schemes, a basic untied social protection fund should be designed that will allow States to pull funds to buttress schemes designed at the state-level, mapped to the broad national strategy. This is similar to the approach of CSS redesign, suggested by the NITI Aayog Chief Ministers' subcommittee on CSS rationalisation and reform.

3. ONE CAVEAT

The institutional home for NEED raises important caveats that need consideration in the long term. The ISC is the obvious home, because it is a political body of CMs and activities such as this fall firmly within its mandate. Second, it has constitutional sanction. However, it is not an autonomous body. The budget for its secretariat is housed within the Home Ministry. Another alternative institutional home could be the NITI Aayog. It has the advantage of having technical expertise within its fold. However, there are disadvantages: a) it is not a political body, b) NITI Aayog is seen as a centralising force which will undermine, at least in terms of signalling, the purpose of this council for deliberation and consensus building, c) its ability to liaison across line ministries (that currently house the CSS) is limited.

Regardless of what the final institutional anchor for the NEED council is, a few core principles must guide its institutionalisation and functioning. These are:

- Establish expectations of the mechanism in advance, in order to ensure consensus building is possible.
- Establish collective executive leadership of the process and the institutions involved.
- Share power and responsibility across States and political parties, to ensure it is seen as non-partisan.
- Establish principles of transparency and participation in process and functioning of the council.

CONCLUSION

The COVID-19 crisis is forcing us to rethink the architecture of the State and the federal distribution of functions. This note is a work in progress in that direction, hopefully, towards a more empathetic, efficient, responsive and resilient State.

FOOT NOTES

- 1 With inputs from Sabina Dewan, Mekhala Krishnamurthy and Srinivas Chokkakula. Views reflected here are of the authors and do not represent an institutional view. Email: yaiyar@cprindia.org
- 2 In FY 2020-21 BE, Gol allocated Rs. 3.40 lakh crore for CSSs. In FY 2021-21 BE, there are over 600 CS schemes with a combined allocation of Rs. 8.32 lakh crore.
- 3 For general category states and 90:10 for north-east and hilly states.
- 4 The Inter-State Council (ISC) although a constitutional body constituted under Article 268 of the constitution, only has recommendatory powers. Moreover, it does not have budgetary authority. Under this conceptualisation, it can reshape its role in the context of a crisis and operate with budgetary powers/ decision making authority working closely with the MoF.
- 5 This is particularly critical as in the next 3-6 months Gol will need to grapple with the challenge of providing migrant workers portable social security. This is critical to incentivise workers to come back to cities and also ensure that the crisis of hunger, witnessed in these last three weeks does not repeat. To do this, the Center and State governments need to on a war footing, put in place a secure, portable food and cash security. One positive fall out of the current crisis is that Chief Ministers, have willingly taken financial responsibility for citizens from their state, while their host state has been entrusted with providing benefits. Domicile States are also experimenting with finding ways of delivering cash to their migrant populations through mobile Apps. These emergency responses need to be institutionalised and could serve as the basis for portability.
- 6 Including allocations under Ministry of AYUSH