FISCAL TRANSFER AND LOCAL DISPARITY IN SOUTH SUMATRA PROVINCE INDONESIA

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HANDOUT

Introduction
Fiscal Decentralization (fiscal transfer)
Local ‘Kabupaten/Kota’ Disparity
Transfer reduce local disparity
Prospect & Challenges
Recommendation
INTRODUCTION

Definition and scope of fiscal decentralization
Issues on fiscal transfer or balanced fund
Fiscal transfer can reduce inequality and disparity
Prospect of fiscal transfer to decrease horizontal imbalance
Best practices on fiscal transfer and decentralization
# Transfer to Regions, 2007-2013

(Billions of Rupiahs)

<table>
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<th>2007</th>
<th>2008</th>
<th>2009</th>
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Why have to Decentralize? (Bahl 1999)

Economic Development
Elected Government
Inefficient Centralization
Uniformity Not Acceptable
Local Government Capacity
Autonomy vs. Backdoor Approaches
Poor Service Delivery
Prevent Secession/Civil War
Why Decentralise? (Devas 2009)

Administrative arguments
- congestion at the centre
- lack of local knowledge at centre
- scope for experiment, innovation, mutual learning

Economic arguments
- greater allocative efficiency if decisions reflect local conditions, needs, priorities
- connecting spending decisions to local tax, thereby internalising costs and benefits

Political arguments
- democratic participation and local choice
- greater access to decision-makers
- increased local accountability
But the dangers

Threat to national unity and power of centre
Lack of capacity at local level
Lack of resources at local level

Risk of increased inter-regional inequality

Risks of inefficiency, loss of coordination and potential for increased corruption

Risks of capture by local elites:
- local decision-making processes not inclusive
- neo-patrimonialism and patronage relationships
- inadequate mechanisms of participation & accountability
Issues on fiscal decentralization

Assigning to which level of governments in the provision of public goods that best internalized benefits and costs (expenditure assignment), and on the assigning revenue sources that mostly efficient among level of governments (revenue assignments).

Transfer or balance fund increase annually

Revenue and purchase of local government also increasing

Majority of province tax (85%) is dominant revenue sharing comparing other sources

Major of local ‘kabupaten’ tax (40%) and retribution (33%) are dominant revenues sharing comparing other sources

Major of local ‘kota’ tax (66%) is dominant revenue sharing comparing other sources
Regional Revenue & Purchase 2008-2013 (National)
Province tax (85%) is dominant source comparing to local retribution
Local ‘kabupaten’ tax (40%) is dominant source comparing to local distribution (33%), excluded asset management (8%), & other genuine
Local ‘kota’ tax (66%) is dominant source comparing to local distribution (14%), excluded asset management (3%), & other genuine
POLITIK DESENTRALISASI DI INDONESIA

Konsep desentralisasi mulai dikenal jaman pemerintah kolonial Belanda Decentralisatie Wet 1903, dijabarkan dalam Betuurshevorming Wet 1922 ada pembagian daerah otonom: gewest, regenschaap, & staatgemeente. 

aman Jepang ketentuan di atas tetap berlaku esudah merdeka, mengacu ke pasal 18 UUD 1945

ahir undang-undang otonomi daerah:

UU No.1 1945 tentang Komite Nasional Daerah dan ketenmtuan pokok Pemerintahan Daerah berlaku sejak tgl 23 Nov 1945

UU No. 22 1948, uu otda pada masa RIS

UDS berlaku dan kembali ke bentuk negara kesatuan, UU No. 22 1948 tetap berlaku

UU No. 1 1957 sebagai uu organik yang baru

Dekrit Presiden 5 Juli 1959 oleh Presiden Soekarno, lahir UU no 6 1959 dan

P No. 1 1963

UU No. 18 1965 tentang Pemerintahan Daerah

aman Orde Baru lahir UU No 5 1974 tentang Pokok-pokok Pemerintahan Di Daerah

UU No. 22 1999 tentang Pemerintah Daerah
DESENTRALISASI FISKAL

Desentralisasi fiskal (DF) adalah pelimpahan wewenang di bidang keuangan dan fiskal kepada daerah dalam memobilisasi dan memanfaatkan sumber-sumber pendapatan daerah. Dengan DF daerah mempunyai wewenang mengatur dan menggali potensi dan sumber2 keuangan sendiri. DF merupakan komponen utama dari desentralisasi. Apabila Pemda melaksanakan fungsinya secara efektif dan mendapat kebebasan dalam pengambilan keputusan pengeluaran di sektor publik, maka mereka harus mendapat dukungan sumber-sumber keuangan yang memadai baik yang berasal dari PAD BHP dan BP, pinjaman, subsidi/bantuan dari Pempus.
FAKTOR PENDUKUNG PELAKSANAAN DF

Pemerintah pusat yang mampu melakukan pengawasan dan enforcement SDM yang kuat pada pemerintah daerah guna menggantikan peran pemerintah pusat

Keseimbangan dan kejelasan dalam pembagian tanggungjawab dan kewenangan dalam melakukan pungutan pajak dan retribusi daerah.
Rasio Dana Perimbangan Thd Pendapatan Daerah (%)

Rasio dana perimbangan terhadap pendapatan daerah kab/kota di Sumsel terlihat perkembangan trend yang berfluktuasi berkisar antara 60% - 90%.
Rasio dana perimbangan terhadap PDRB kab/kota di Sumsel untuk melihat besarnya dana transfer yang dapat menstimuli ekonomi daerah di masing-masing kabupaten/kota.
Elastisitas alokasi dana transfer terhadap pertumbuhan ekonomi kabupaten/kota di Sumsel bersifat tidak elastis berarti ini justru menimbulkan...
DISPARITY

Higher local economic growth can stimulate higher local disparity.
Different fiscal transfer can increase fiscal gap among local governments because they stimulate different implication on local revenue and local purchase of budget.
Transfer of fund can reduce disparity among local government through priority allocation on education, health, and infrastructure.
Fiscal transfer may reduce economic disparity among local but slow result empirically.
Theories of Regional Disparities and Development

Three main theoretical approaches:

– Neo-marxist, theory of “underdevelopment”
– Neoclassical economics
– Institutional political science
Neo-Marxist Theory

Class-based analysis of society and politics

Ownership and spatial concentration of wealth is important

Structure of development versus underdevelopment: regions are “kept” undeveloped or underdeveloped

International application, but also within a large country such as Canada Metropolitan-Hinterland a variant of this
Neoclassical Economics

The market is (or should be) what determines development.

Geographic and natural resource development help determine economic distribution of resources.

The free market will adjust labor and capital to promote optimal allocation of resources.

Economic integration and trade patterns important to consider.

More recently: human capital formation seen as important factor.
Institutional Theory

Politics and the shape of institutions drive economic outcomes.
Policy factors shape the economy over time.
Markets (and their rules) are themselves institutions.
In a regionally diverse economy, some regions win, some lose, according to their political influence and input to institutions.
Figure 3.2: Regional disparities within non-industrial countries
Transfers to reduce regional fiscal disparities (Shah, 2004)

**Design:** General non-matching fiscal capacity equalization transfers.

**Better practices:** Fiscal equalization programs (*sources of data: CGC, Finance Canada, Lotz, Shah & Spahn*)

- Paternal: Australia (fiscal capacity plus fiscal needs) and Canada (fiscal capacity only)
- Solidarity, Fraternal or Robin Hood: Germany (fiscal capacity), Sweden, Denmark

**Practices to avoid:** General revenue sharing with multiple factors e.g. practices in Brazil, India and South Africa
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<td>2013</td>
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Comparing Gini ratio between South Sumatra and Indonesia tend to higher.
Indeks Williamson dan Indeks Theil untuk Total Dana bagi Hasil Kab/Kota di Sumatera Selatan, 2001-2008 (%)

Disparitas keuangan daerah mempunyai trend naik berarti semakin 
par; (2) pembagian dana bagi hasil belum berfungsi menutupi 
kepemimpinan yang terdesentralisasi yang semakin jelas; (3) indeks
### Isi Cohen korrelasi antar variabel keuangan daerah kab/kota Sumsel

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<td>-0.712*</td>
<td>-0.659**</td>
<td>-0.776*</td>
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<td>0.058</td>
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<tr>
<td>Covariance</td>
<td>-0.016</td>
<td>-0.007</td>
<td>0.010</td>
<td>0.024</td>
<td>0.062</td>
<td>0.030</td>
<td>0.008</td>
</tr>
<tr>
<td>N</td>
<td>8</td>
<td>8</td>
<td>8</td>
<td>8</td>
<td>8</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Pearson Correlation</strong></td>
<td>0.779*</td>
<td>0.385</td>
<td>-0.845**</td>
<td>-0.890**</td>
<td>-0.889**</td>
<td>-0.884**</td>
<td>1</td>
</tr>
<tr>
<td>Sig. (2-tailed)</td>
<td>0.023</td>
<td>0.346</td>
<td>0.008</td>
<td>0.003</td>
<td>0.004</td>
<td>0.004</td>
<td></td>
</tr>
<tr>
<td>Sum of Squares and Cross-products</td>
<td>0.014</td>
<td>0.008</td>
<td>0.004</td>
<td>0.003</td>
<td>0.004</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

* Significant at the 0.05 level (2-tailed).
** Significant at the 0.01 level (2-tailed).
Implikasi Koefisien Korelasi

Koefisien korelasi antara rasio PAD/Dana Perimbangan dengan indeks Williamson DAU sangat signifikan yaitu sebesar –0,859. Hal ini berarti semakin kecil rasio PAD/Dana Perimbangan, maka disparitas keuangan berdasarkan DAU semakin besar.

Korelasi antara PAD/PDRB dengan indeks Williamson DAU sebesar -0,776, ini berarti semakin tinggi rasio PAD/PDRB, maka indeks Williamson semakin rendah.

Korelasi antara indeks Williamson dengan derajat sentralisasi fiskal sebesar -0,779, ini berarti semakin tinggi derajat sentralisasi fiskal, semakin tinggi.
Best Practice: Fiscal Federalism
(Brown, 2009)

Fiscal Federalism (FF) = The system of revenue sharing, expenditure sharing, and direct intergovernmental transfers in any multi-level government political community

Fiscal Equalization (FE) = A Federal government program to top-up the revenues of provinces with below-average fiscal capacity

Equalization provides unconditional grants to the recipient provinces--allows provinces the autonomy to spend as they like...to alleviate disparities in basic service

Canada Health Transfer (CHT)...it and other federal transfer programs (intergovernmental grants) are more or less conditional...i.e., funds are for a specified
Fiscal transfer can stimulate local economic growth.

Transfer of fund have to manage efficient and effective to overcome local disparities.

The local budget focus on priority program to decrease the inequality.

Fiscal transfer improve local revenue to finance many programs and projects to increase local growth and to reduce disparity.
Fungsi APBN (DJPK 2013)

Fungsi alokasi: Fungsi alokasi pada dasarnya adalah menggunakan berbagai sumber pendapatan untuk menyediakan pelayanan publik.

Fungsi distribusi: Pendapatan negara dari pajak dan bukan pajak tidak semua digunakan secara langsung untuk menyediakan pelayanan publik. Tetapi dapat juga didistribusikan dalam bentuk dana subsidi dan dana pensiun.

Fungsi stabilisasi: APBN sebagai ujud kebijakan fiskal bersama-sama kebijakan moneter berfungsi untuk menjaga stabilitas harga, stabilitas nilai tukar, dll.
Fungsi APBD

Fungsi Otorisasi: dasar untuk melaksanakan pendapatan dan elanja pada tahun yang bersangkutan.

Fungsi Perencanaan: pedoman bagi manajemen dalam herencanakan kegiatan pada tahun yang bersangkutan.

Fungsi Pengawasan: pedoman untuk menilai apakah egiatan penyelenggaraan pemerintah daerah sesuai tentuan yang ada.

Fungsi Alokasi: mengurangi pengangguran dan pemborosan umber daya, serta meningkatkan efisiensi dan efektivitas erekonomian.

Fungsi Distribusi: memperhatikan rasa keadilan dan epatutan
Hubungan APBN–APBD (DJPK 2013)

Penerimaan Pemerintah:
- Penerimaan Dalam Negeri
  - Pendapatan Asli Daerah:
    - Pajak
    - Bukan Pajak
  - Transfer dari Pemerintah Pusat

Belanja Pemerintah:
- Belanja Pemerintah Propinsi
- Belanja Pemerintah Pusat
- Belanja Daerah:
  - Pem. Propinsi
  - Pem. Kabupaten/Kota

Pembiayaan:
- Pinjaman

Penerimaan Propinsi:
- Pendapatan Asli Daerah:
  - Pajak
  - Bukan Pajak
- Transfer dari Pemerintah Pusat

Belanja Pemerintah Propinsi:
- Belanja Pem. Propinsi
- Belanja Kabupaten/Kota

Penerimaan Kabupaten/Kota:
- Pendapatan Asli Daerah:
  - Pajak
  - Bukan Pajak
- Transfer dari Pemerintah Pusat
- Pem. Propinsi

Hubungan APBN–APBD (DJPK 2013)
CHALLENGES

Many constraint and implication to reduce disparity by using pattern of fiscal transfer
Weaknesses of local government management is the main constraint
Ego sector and hard coordination influence on many local development program and activities
Lack of fund and local distress are beyond in order to eliminate local disparities
Indirect local purchases (*operational expenditure*) is bigger than direct purchases (*capital expenditure*)
Intergovernmental Fiscal Transfer Reduction of Regional Fiscal Disparities (Fleiner, 2003)

Three objectives:

- Bridging vertical fiscal gaps
- Bridging fiscal divide between nations
- Securing a common economic union through establishing national minimum standards in social and infrastructure services
APPLICATION:
Clarity and consensus for responsibilities
Finance should follow function to strengthen responsibilities
To ensure fiscal discipline all governments must be made to face the fiscal consequences of their decisions
Securing a common economic union through unimpeded goods and factor mobility and national minimum standards for social services and infrastructure is the best guarantee for political and economic stability & regional convergence.
Properly designed intergovernmental transfers can strengthen results based accountability and also enhance competition for the supply of public goods, fiscal harmonization, state and local government accountability, and regional equity.
Institutional arrangements for managing intergovernmental
Intergovernmental Transfer (Bahl 2012)

- Intergovernmental transfers
  - Grants
  - Subsidies
  - Shared taxes
- Local taxes
- Piggyback local taxes
Types of Intergovernmental Transfers

- Unconditional or general
- Conditional or specific (for capital and/or operating expenditures)
  - Non-matching
  - Matching
    - Open-ended
    - Close-ended

Direct cost reimbursement
Justifications for Intergovernmental Transfers

Close the “fiscal gap” (More Transfers, More Local Raised Revenue, Local Expenditure Efficiency, Re-Assign Expenditure/Responsibility)

Equalize fiscal capacity and need (The objective of an equalization transfer should be to protect (or guarantee?) some basic level of services)

Adjust for spillovers (Fiscal Capacity, Expenditure Needs, Capacity-Needs Gap)

Increase effectiveness of central expenditures

Political reasons
The Transfer System has a Strong Effect on Fiscal Disparities among Sub-National Governments (Schick 2011)

Decentralizing public finances risks enlarging inequality among Sub-National Governments (SNGs) because rich local governments can generate more tax revenue than poor governments.

The transfer system (return of tax revenue and grants) can either widen or narrow these disparities. Tax rebates (or sharing) returns more to affluent communities with strong tax bases, and therefore has counter-equalizing effects: a formula based system (for example, with the amount transferred verse to per capita income) has the potential to narrow fiscal differences among SNGs.

Grants also have the potential to expand or reduce inequality. Grants that match local expenditures tend to be de-equalizing, those that compensate SNGs for low income have the opposite effect.

is important for Central Government (CG) to periodically review the
Negative Lessons: Practices to Avoid (Shah 2004)

General revenue sharing with multiple factors
Deficit grants
Fiscal Effort Provisions
Input or process based or ad hoc grants
Capital grants without assurance for upkeep
Negotiated or discretionary transfers
Positive Lessons: Practices to Strive For (Shah 2004)

K.I.S. (keep it simple)
Focus on single objective
Introduce sunset clause
Output based conditional transfers with citizens’ evaluations
Fiscal capacity equalization to a defined standard
Political consensus on the standard of equalization
Institutional arrangements for broad based
RECOMMENDATION

Fiscal transfer system on local government is important to help and make widespread local financing but doesn’t make impact on narrowing fiscal gap among ‘kab/kota’ in South Sumatra. The higher fiscal dependency degree, the local government couldn’t make improve the capacity themself on local revenue. Fiscal transfer may reduce the local disparity but the realisation is very slow empirically. Implication of fiscal transfer maybe can reduce disparity but also stimulate a higher disparities.
Bahl, Roy, 2014. ‘Intergovernmental Transfers’, Georgia State University (rbahl@gsu.edu)


Fileiner, Thomas. 2003. ‘Fiscal Decentralization,’ ...

Allan Schick, 2011. ‘Fiscal Decentralization: Governing for Results’, Special Course on Impact Evaluation and Results-Based Planning and Budgeting, Shanghai, 14-18 November.

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