

Fiscal Decentralization after Implementation of Local Government Autonomy in Indonesia

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This research aims to explain the relationship between local fiscal capacities, intergovernmental transfers with the realization of the budget. Using the sample budget of 190 districts in Indonesia, three hypotheses have been tested. The results of this study indicate a high dependence of local governments, to grants from the national government. Although there are close links between local fiscal capacities with performance budgeting, intergovernmental transfers are not fully mediating the relationship.

Keyword: Local own revenue, grants and transfer, local government budget

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1. Introduction

After application of local autonomy and fiscal decentralization, national governments seem unable to achieve its objectives. The government's efforts to improve the fiscal capacity of regions, which is done by allocating grants to local governments, seems to have not succeeded (Harryanto, 2009). Under the law, the allocation of grant has the objective, which includes to improve and to balance the fiscal capacity of regions. However, until 2009, unequal distribution of the local fiscal still exists. Revenue obtained from taxes and levies have not achieved an equal distribution, and even unable to finance the salary and wage expenses (Harryanto, 2009).

The imbalance of fiscal capacity of the regions is determined by the difference in views between the national and regional governments. In the perspective of the national government, as has been mentioned in the statute, the allocation of subsidies and grants are used to enhance the ability of regions to finance the needed public services, and to organize and keep pace regional development. In terms of the local government view, before the implementation of regional autonomy, the central government has received such benefit from the exploiting local resources, so in this era of autonomy, the central government has to pay back what has been delayed.

There are different ways of looking at the transfer, which creates a variety of local efforts that bring the results of development in the era of autonomy. Several studies (Pambudi, 2008; Firdausy, 2004) showed that local financial imbalances have forced local governments to encourage their income sources by developing new taxes and levies. By increasing the income sources in excess, causing the local economic development to be hampered.

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This raises a research question; "Is the allocation of national government in the form of grants, and transfer has not been able to raise the local fiscal capacity?" This question comes after the allocation of grants by the national government has met large amounts. If we compared with its local own revenue, the transfer is more than 50% of the total revenue. In addition, this allocation has been done nearly ten years. Therefore, conclusion should have been drawn now.

This research attempts to explain the empirical findings of the relationship between local fiscal capacity, which affects the budget, and grants. This also incorporates a mediating variable in that relationship. Using secondary data from 190 districts in Indonesia, this study apply the method of hierarchical regression analysis to test three hypotheses. The first hypothesis presented in this research is to examine the relationship between local fiscal capacities with the grants and transfer. Second, the relationship between the grants to the budget performance, and third, combining the three variables simultaneously.

2. Theoretical Framework

There have been many theories and concepts, which explain the government's budgetary position in relation to public accountability. In democratic countries, governments do not just draw up the budget for the given tasks between levels of government, but also accountable to the public. Illustrating the agency relations applied in the government organizations appear to be a complex relationship, because not only explain the relationship between government and the public and legislators, but also in the organization of government itself, such as between the superior and subordinate government.

2.1 Agency Theory

Agency theory has been used to explain the complex relationships between various government agencies. The relationship between the public as voters with the executive government, the relationship between the legislature with the executive, and the relationship between government superiors and subordinates, has also been described by using the theory of agency (Mulgan, 2000; Shi & Svenson, 2002; Lupia, 2001).

In government organizations, especially between the national government and the local government, there is a principal agent relationship, where the national government is a principal and local government as an agent. The relationship appears first with the regional autonomy where local government is the existence of a political process. Local government leaders are directly elected from the electoral process area (local election). However, Indonesia as a unitary state, the local government is responsible, in addition to the local community as a voter, but also responsible to the national government.

The agency relationship leads to exist on the asymmetric information, which brings some behaviors such as opportunistic behavior, moral hazard, and adverse selection. Opportunistic behavior that appears in the budgeting process: firstly is explicit in the

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budget the so-called public-oriented budget. The programs incorporated into the budget contain underlined public-oriented, and actually contains the government's interest to finance short-term needs.

Secondly, the allocation programs into the budget that could put the government more powerful in its political position, especially for the upcoming electoral process (Mulgan, 2000). Programs that are attractive to local voters are placed in the budget, and the public can participate in it.

The elaboration above concerning the agency theory may pervade budgeting process in government organizations. The fact that through agency theory, the executive is an agent between the legislature and public and legislature is an agent from public as voters. The position of legislature as representative of the public, in the occurrences of asymmetry information may cause opportunistic behavior such as adverse selection and moral hazard (Shi & Svenson, 2002).

The explanation above point out that the agency theory is used in the budgeting process, especially for the government organizations. Agency theory explains that the executive is an agent of the public and the legislature, and the legislature is an agent of society as a voter. The position of the legislature as a representative of the community, in the event of asymmetric information can lead to opportunistic behavior such as adverse selection and moral hazard (Shi & Svenson, 2002).

Empirical research by Lewis (2005) showed that the revenues derived from taxes and user charges are directly influenced by the presence of dependence on intergovernmental transfers. Meanwhile, the study of Saad (2002) and Pambudi (2008) showed that there are tax efforts by local governments that can hamper the regional economy.

2.2 Accountability

Accountability is as not only a responsibility to do reports on what has been done, but also to prevent abuses of authority that has been gained. Parties who receive authority to carrying out its activities will have the complete information of what has been done. While the party providing the authority have incomplete information. Therefore, if there is mutual distrust, there arose what is called the cost of accountability.

Accountability is used to strengthen the application of agency theory in explaining the phenomenon of public budgets. Principal-agent relationship is strengthened by the concept of accountability. An agent has an obligation to the principal, and the obligation is called accountability. In the government organizations, the relationship between the government and public institutions is characterized by existence of interest parties, which can be classified as principal and agent. Some parties act as principals, and others as agents. This creates the concepts of accountability, such as political accountability, public accountability, and financial accountability (Mack & Ryan, 2002).

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Financial accountability asserted that the implementation of government financial management is based on the interests of the people as provider of the mandate to the government that is to plan and implement the budget. Budget in favor of the people is the budget not only in terms of expenditure, which meets the allocation of public services as expected, but also from the revenue side.

Public budgets have an influence on economic activity. In terms of revenues, public budget can be used to build a conducive of business climate, and to invigorate of the economic sector grow. However, the consequences of local revenue may also be obstacles to business and economic climate.

Public budgets have an influence on economic activity. In terms of revenues, public budget can be used to build a conducive of business climate, and to invigorate of the economic sector to grow. However, the consequences of local revenue may also bring obstacles to business and economic climate. From the expenditure side, spending for the provision of public goods, especially infrastructure will build a huge opportunity movement of people's economic sectors. Public services such as facilitating, regulatory, and development of the business sector strongly supports the creation of good business climate.

Norton and Elson (2002) suggest that an important foundation of accountability is the shared decision of the government and society in the budget setting process. Besides, Mack and Ryan (2002) argued that the accountability of government organizations become more important than decision usefulness.

Public budgets technically are composed of budget revenue and spending. However, their existence has implication to the public. On the side of the budget revenues, revenues derived from taxes and levies to the community, and explore and exploit natural resources carry a negative externality on society. On the expenditure side, the budget includes the provision of public infrastructure, which should then be subject to levy for public use; in essence to provide direct and indirect impacts to the community. The revenue led expenditures approach that emphasized the determination of public budget, which begins, with the determining of the revenue budget, and followed by the setting of spending. Budget revenue starting with the income derived from its own resources, grants and lending.

The most important government revenue is derived from its own resources in the form of taxes and user charges. In the government organizations, there consists of superior and subordinate government. Local government is subordinate of national government, and the revenues not only come from local taxes and charges, but also come from the national government in the form of grants, and tax and transfer. The fiscal relationship between national and local government is arranged in the policy that is called fiscal decentralization.

2.3 Fiscal Decentralization

Fiscal decentralization is a process of delegation of authority from central to local governments. There are two approaches in the delegation of these powers. The first is where the central government collects revenues from these revenue sources and then performs the division of revenue to local governments. The second approach is where the local governments collect the revenue, and then share to the central government.

The Indonesian government conducted a mixture of approaches: 1) There is revenue collected by the central government and then shared with the local governments, 2) there is delegated collection of revenue to local governments but still distributed by the central government, and 3) there is a collection of local revenue and its use is fully delegated.

Revenues of central government are then redistributed to local governments in the form of grants and transfer. Implementation grants allocation policy is set by law (Law No.32, 2005). The general goals of Indonesia's fiscal decentralization program are to help (Sidik & Kajatmiko, 2004):

- (1) increase national allocative and regional government operational efficiency;
- (2) meet regional aspirations, improve overall fiscal structure, and mobilize regional and therefore national revenues;
- (3) enhance accountability, increase transparency, and expand constituent participation in decision-making at the regional level;
- (4) mitigate fiscal disparities among regional governments and assure the delivery of basic public services to citizens across the country;
- (5) ameliorate social welfare of Indonesians; and
- (6) support macro-economic stability.

2.4 Local Revenues

Government revenues consist of taxes and levies imposed on the community. With the implementation of fiscal decentralization, the taxes and levies are separated according to their characteristics. Certain taxes and charges will be retained at national government level, and some delegated to local governments. Revenues derived from taxes and levies, which has been delegated is called local own revenue.

Revenue is the revenue of local government established through local legislation, managed, and used by local government decisions. Revenue is an important source of local government because it is collected and used without due process of the central government bureaucracy.

In addition from the local own revenues, transfer and taxes is also a regional income. These revenues are different from local revenues, in terms of the management and the utilization. The transfer is derived from natural resource management, such as the exploration of oil and gas, forest products, mining, and fisheries. The results from the

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management of those resources are collected by the central government and redistributed to local governments in accordance with the law.

Part of the transfer is distributed with a greater proportion to the central government such as oil and gas. Others, such as forest management, mining, and fisheries are distributed with a greater proportion to local governments. Transfer is still not transparent, because the entire management is set by the national government. The local government knows only the figures after the national government decided on the allocation.

Management of tax and transfer is carried out by the central government and distributed to local governments under the legislation. The taxes belonging to the transfer and is in accordance to its characteristics is a local tax. Characteristics of local tax are the tax is permanently located in the region, such as property tax, individual income tax, and tax changes in property ownership. These taxes have a transparent mechanism and bureaucracy is relatively easier.

Local government revenue comes from central government transfers are also in the form of grants. There are two types of grants, which are the General Purpose Grant and Specific Purpose Grant. Assessment of the magnitude of the proportion is regulated through national legislation, but the allocations to each local government are done by a method and formulation is carried out by the national government.

The three forms of transfer including tax and transfer, the General Purpose Grant, and Specific Purpose Grants can be categorized as intergovernmental transfers. Intergovernmental transfers are much larger amounts than the local revenues (Ministry of Finance Office, 2009). Hence, the reliance on transfers of the local government becomes very important. Some research (World Bank, 2007; Asian Development Bank, 2007) indicates that revenue from the districts and cities have not been able to finance expenditures to pay salaries and wages of the employees.

Based on the above discussions, three hypotheses have been developed:

1. Grants and Transfer significantly affects the local own revenue.
2. Local Own Revenue significantly influences the budget performance.
3. Grant and Transfer significantly influences budget performance mediated by Local Own Revenue.

3. Method of Analysis

Local governments in Indonesia consists of provincial, district and city. Provincial governments have different degrees of local autonomy with the district and city while the districts and cities have similar degree of autonomy. This study discusses the budgets of local governments. Thus, the sample used is only district. The number of districts and city in Indonesia in 2010 is 488 counties. Samples are taken by using cluster random sampling method, and 192 districts selected.

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In order to test the hypothesis, hierarchical regression is used, which is preceded by reliability testing with Cronbach's Alpha, the validity of the Keizer Meyer Ohlin (KMO) and Principal Component Analysis (PCA), and testing of linearity with Skewness and Kurtosis.

Budget Performance = f(Expenditures), and Expenditures = f(Revenues)

Budget performance = f(Revenues)

Revenues = f(Local Revenues, Grants and Transfer)

Budget Performance (BP) = f(Local Revenues (LR), Grants and Transfers (GT))

Therefore:

$$BP = \alpha_0 + \alpha_1 LR + \alpha_2 GT + \epsilon$$

For the purpose of test the hypotheses, the equation used is as follows:
For hypothesis 1

$$GT = \alpha_0 + \alpha_1 TR + \epsilon$$

For hypothesis 2

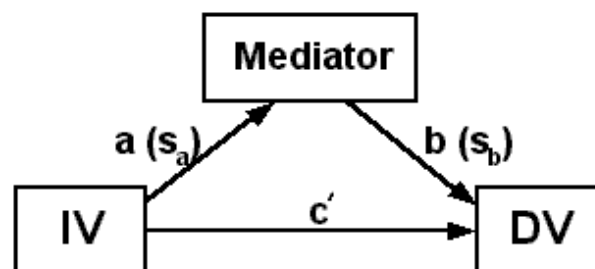
$$BP = \beta_0 + \beta_1 GT + \epsilon$$

For the hypothesis 3

$$BP = \gamma_0 + \gamma_1 LR + \epsilon$$

To test the mediating effect of Local Revenue to the budget performance used Sobel parameter test (Preacher & Leonardelli, 2010). The mediation relationship of the variables refers the following this structure.

Graph 1: Mediating Variable



With statistical test used the formula as follows:

$$\text{Sobel} = a * \left(\frac{b}{\sqrt{(a^2 s_b + b^2 s_a)}} \right)$$

Where:

a = regression coefficient of Local Revenue

Sa = standard error of regression coefficient of Local Revenue

b = regression coefficient of Grant and Transfer

Sb = standard error of regression coefficient of Grant and Transfer

4. Results

4.1 The Local Government Revenues

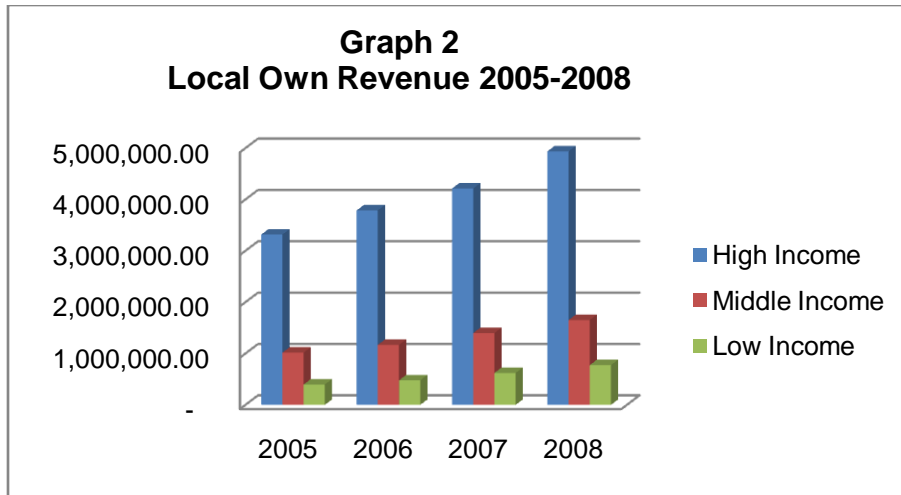
A time series of district government revenue from 2005 to 2008 is shown in Table 1 below:

Table 1: Local Own Revenue of High, Medium and Low Income of Regencies 2005 to 2008 (in percentage)

No.	Regencies	Local Own Revenue			
		2005	2006	2007	2008
1	High Income	70.11	69.69	67.60	67.05
2	Middle Income	21.51	21.51	22.43	22.43
3	Low Income	8.37	8.80	9.97	10.52
Total		100.00	100.00	100.00	100.00

Source: Finance Ministry Office, 2005 - 2009

Based on its local own revenue, the districts can be divided into three groups: high-income, medium-income, and low-income districts. Table 1 above shows that in 2005, the high-income districts have contributed 70.11% of total local own revenue to the total national. Only 21.51% has been contributed by middle-income district, and only 8.37% of low-income districts. 2008 seems to have been a shift in which the high-income districts have contributed less if comparing to that of in 2005. These contributions amounted to 67.05% for the high-income district, 22.43% for middle income, and low income 10.52%.



Source: data processed by Author

Comparing the three groups of these districts, they appear that the income gaps between the districts are quite large. The high-income district contributes more than half the national total. Meanwhile, both middle-and low-income groups, although both the income of the district is added, the figure is still less than half the national total. Viewed from its development during the year 2005 up to 2008, the composition remains unchanged.

Table 2: Grants and Transfer of High, Medium and Low Income of Regencies 2005 to 2008 (in percentage)

No.	Regencies	Grants and Transfer			
		2005	2006	2007	2008
1	High Income	49.45	47.34	47.50	47.13
2	Middle Income	31.87	31.76	31.41	31.88
3	Low Income	18.68	20.90	21.09	21.00
	Total	100.00	100.00	100.00	100.00

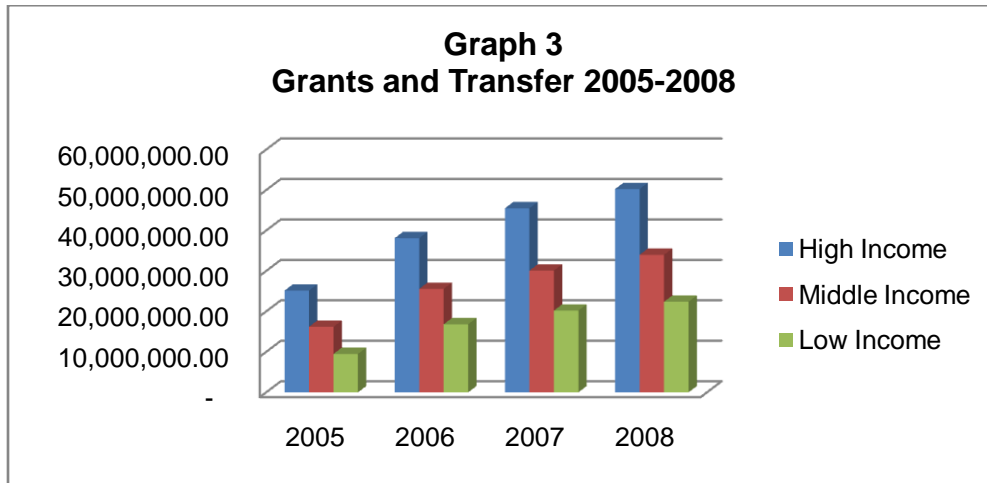
Source: Finance Ministry Office, 2005 - 2009

In addition, from the local revenues, the local governments still have an income that is derived from the national government that is grants and transfer. Grants consist of general-purpose grants and specific purpose grants, and transfer made up of Revenue and Tax Sharing. Table 2 shows the time series of grants and transfer during 2005 to 2008. In 2005, the high-income districts have absorbed of 49.5% of the total national allocation. While the middle-income districts have absorbed of 31.87%, and the low income districts have absorbed of 18.68%.

In 2008, there was little change in the distribution of grants and transfer, in which the high-income districts absorbed 47.13% of the total national allocation. While the middle-income districts absorbed 31.88%, and the low-income districts absorb only 21% of the national total. Time series data from 2005 to 2008 indicates that the high-income

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districts decreased in proportion, while the low-income increased and the middle-income is relatively constant. This illustrates that the distribution have improved to a more equally distributed during 2005 to 2008.



Source: data processed by Author

From the Graph 1 and 2, Comparison between both the distribution of local own revenue and the distribution of Grant and transfer seem that the distribution tends to form similar pattern in which the highest income received higher allocation while the low income received lower allocation. However, the equalization of the distribution is different. The local revenue gap between the high income and the low income was very high, while the grants and transfer the gap was not so high.

Table 3: Summary of Local Own Revenue, and Grants and Transfer of High, Medium and Low Income of Regencies (in percentage)

	Local Revenues	Grants and Rev. Sharing
High-Income	68	43
Middle-Income	23	33
Low-Income	10	24
	100	100

Source: Finance Ministry Office, 2005 – 2009

Table 3 shows the summary of local revenue and grants from the high-income, middle income and low-income districts. As shown in the table, the distribution of local own revenue showed a high disparity. This is illustrated by the contribution from local own revenue from the high-income, which produced more than 50% of the total national, while the sum of both middle-and low-income districts is lower than 50% of the total national.

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Meanwhile, the distribution of the grants and the transfer appear to be more equal. The high-income district absorbs 43% of the total national allocation, 33% the middle-income and the low- income absorb only 24% of the total national allocation.

If we refer to the purpose of allocating grants and transfers that are encouraging local own revenue to increase and financial capability of the region, which is distributed more equitably, then the question arises: “have these objectives been satisfied”? To answer this question, then the inference analysis to test the hypothesis as has been proposed in this paper.

4.2 Relationship between Local Own Revenues, Grants, and Transfer

The relationship between local revenues, grants and transfer on the performance of the budget, theoretically explained that government spending could affect the regional economy through the growth of the sector-sector and regional revenues. Further increase in the local economy will have an influence on local income especially local revenues.

In connection with the above objective, three hypotheses have been advanced, as has been stated before. The hypotheses are (1) Grants and transfer has a positive and significant impact on local revenues, (2) grants and transfer have an influence on the performance of the budget, and (3) Local revenue and grants and transfer has a positive and significant influence on the performance of the budget.

Nevertheless, before the hypothesis is tested, a descriptive of the variables are presented in the following Table 4.

Table 4: Descriptive Statistic of the Data

Items	2005	2006	2007	2008
Local Own Revenue				
N	192	191	192	192
Minimum	604.40	788.00	2,636.78	4,044.00
Maximum	329,073.61	269,730.84	353,367.49	449,676.00
Mean	24,509.52	28,258.73	32,228.52	38,285.43
Std. Deviation	33,508.58	37,401.74	40,198.55	47,555.05
Grants and Transfers				
N	192	192	192	192
Minimum	66,050.00	181,586.52	222,399.52	154,566.00
Maximum	749,874.04	975,556.54	1,280,997.43	1,303,941.00
Mean	262,546.80	414,699.75	493,368.91	549,040.26
Std. Deviation	113,942.08	153,640.54	186,950.28	205,872.41

Table 4: (continued)

Budget Performance				
N	192	192	192	192
Minimum	88,759.57	88,759.57	199,503.32	200,471.70
Maximum	1,125,045.23	1,271,641.07	1,624,534.56	1,866,522.13
Mean	355,107.45	455,792.05	513,691.59	610,786.32
Std. Deviation	173,305.50	186,217.11	211,541.39	264,907.33

Source: Local Government Budget 2005-2009, data processed

Table 4 shows the data description of the local-own revenue (LOR), grants and transfer (GAS), and budget performance. Local own revenue have uneven distribution that can be seen from the comparison between the mean and standard deviation. In 2005, an average of LOR is 24,509.52 and the standard deviation is 33,508.58. This comparison showed that there still exists a great variation among local governments LOR. The large variation exists because the value of standard deviation is greater than the mean. In 2008, the mean was 38,285.43, the standard deviation is 47,555.05, and this still shows a great variation. Therefore, it can be said that the changes that led to the improvement of distribution has not occurred, and a very large variation between regions is still happening.

Table 4 also describes the distribution of GAS. Distribution of GAS seems to differ with the LOR. From 2005 until 2008, the average value is never greater than the standard deviation. This shows that there is no great variation in the distribution. Budget performance is expected to ensure regional economic growth, which also experienced a similar distribution with GAS. During 2005 to 2008, the average value of the performance of the budget is always greater than the value of standard deviation. This illustrates that the variation between districts is not too big.

Table 5: Coefficient of Regression and Significant Level of Variables

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
	1 (Constant)	10.4298	0.185		
Local Own Revenue	0.276	0.0193	0.7133	14.0284	0.00**)
a Dependent Variable: Budget Performance R = 0.713, R ² = 0.509					
1 (Constant)	9.252	0.211		43.909	0.00**)
Local Own Revenues	0.328	0.022	0.735	14.921	0.00**)

Table 5: (Continued)

a Dependent Variable: Grants and Transfer R = 0.735, R ² = 0.540					
1	(Constant)	3.455	0.321	10.770	0.00 (**)
	Grants and Transfers	0.772	0.026	0.908	29.815 (**)
a Dependent Variable: Budget Performance R = 0.91, R ² = 0.82					
1	(Constant)	10.430	0.185	56.337	0.00 (**)
	Local Own Revenues	0.271	0.019	0.713	14.028 (**)
2	(Constant)	3.871	0.366	10.573	0.00 (**)
	Local Own Revenues	0.038	0.017	0.101	2.278 (0.02 *)
	Grants and Transfers	0.709	0.038	0.833	18.780 (**)
a Dependent Variable: Budget Performance R = 0.71, R ² = 0.51 R = 0.91, R ² = 0.83					

**) significant at $\alpha = 0.001$, *) Significant at $\alpha = 0.05$

Source: Local Budget 2005-2008, data processed

Table 5 above shows the results of statistical tests as follows:

- 1) Independent variables LOR is positive and significant influence on the Budget Performance with $R^2 = 0.51$, B = 0.271, significant at $\alpha = 0.001$.
- 2) Independent variables LOR are positive and significant effect on GAS with $R^2 = 0:54$, B = 0.328 significant at $\alpha = 0.001$.
- 3) Independent variables GAS is positive and significant effect on budget performance, with $R^2 = 0.82$, B = 0.772 significant at $\alpha = 0.001$.
- 4) The next testing is used a hierarchical regression method. This test is to simultaneously regressing between the LOR and the GAS as independent variables, and the budget performance as dependent variable. Statistical test results point out that in model 1, LOR in a positive and significant effect on budget performance, with $R^2 = 0.51$ with B = 0.271, significant at $\alpha = 0.001$. While in model 2, taken together these two independent variables has a positive effect of performance budget. Coefficient of regression of the LOR is 0.038 and

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the significant level $\alpha = 0.05$. While the GAS has the coefficient of regression is 0.709, significant at $\alpha = 0.001$

- 5) Based on these four tests can also be said that the GAS as a mediator of the relationship between LOR with budget performance.

5. Discussion and Concluding Remarks

Empirical test results indicate that the local own revenue is positive and significantly influence the budget performance. These results are in accordance with the recommended and expected by the national regulation (Sidik & Kajatmiko, 2004), and the results of empirical studies by Lewis (2005). However, some researchers (Brojonegoro, 2004; Bayhaqi, 2004; Firdausy, 2004) argued that the local governments are still shrouded in various capacity constraints. Brodjonegoro and Mahi (2003) argued that local governments have no significant capacity. While Firdausy (2004) argued that fiscal decentralization, have implications for the emergence of local taxes that have proliferated, levy a burdensome and restrictions on business and trade. Similarly, Pambudi (2008) points out that fiscal decentralization brings about interference to the business, taxes and levies ignore the creation of a conducive of business climate.

Meanwhile, the results of this study suggest that the local fiscal capacity, which is reflected from the local own revenues have not distributed evenly across the country. Inequality of the capacity was still pushing the local governments to impose tax efforts. These efforts are impeded the local economic growth.

Local own revenue, and grants and transfer, each individually, have a significant effect on the budget performance. This finding is also supported by previous researches (Lewis, 2005; Sidik & Kajatmiko, 2004; Brodjonegoro, 2004). Local own revenue is a representation of the capacity of local financial resources. As a regional resource, this includes natural resources, human, and technology. The results of local resource management, whether for business purposes or for the purposes of infrastructure development, have an effect to the fiscal capacity for both locally, and nationally.

Local fiscal resources are relatively more limited (Bayhaqi, 2004) and is very critical to developed, as it relates to economic activity (World Bank, 2007). The higher local taxes imposed on society, certainly can reduce the ability to expand their businesses (Pambudi, 2008).

The greater resources held by national governments (Firdausy, 2004), as the result of oil and gas processing, forestry and plantations, the greater revenues are obtained. Nevertheless, this will create conflicts of interest because the exploitation of these natural resources will leave the cost to local communities, while the great benefits gained by the national government (Sidik & Kajatmiko, 2004). Differences of interest cannot be bridged by the grants and transfer (World Bank, 2007). There is always an obstacle in encouraging the creation of a balance between local fiscal capacities, as expected by law (Law No.32, 2005).

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Implications of fiscal resources held by the central government are the existence of a very high level of local dependence on the transfer (Lewis, 2005; Sidik & Kajatmiko, 2004). Although Lewis (2005) suggests that there is no empirical evidence that reliance on transfers cause local governments to develop new tax sources. However, the results of several studies (Firdausy, 2004; Pambudi, 2008) show different things. Recent observations (Pambudi, 2008) still shows there are still many regions levies in the form of user charges that are not clear designation.

Simultaneously both the independent variable local own revenue, and grants and transfer has a positive and significant impact on budget performance. This finding is supported by previous researches (Lewis, 2005; World Bank, 2007; Asian Development Bank, 2004). Under the law, that local own revenue is used to finance the needs for public services, while grants and transfer is used to help the fiscal capacity of improving public services and regional development (Sidik & Kajatmiko, 2004). However, in fact, the regions relies heavily on financial transfers (Lewis, 2005), and significant sources of income in the hands of central government (Firdausy, 2004; Bayhaqi; 2004). Therefore, it is unavoidable to make the transfer of local government as the main financial sources. This means that the effort of the national government to encourage the local own revenues have not been achieved.

Finally, it can be concluded that the experience of regional autonomy with fiscal decentralization policy has encouraged local governments to increase regions fiscal capacity. However, the unavoidable dependence of local governments to transfer from national government is still very high. The situation is still carrying the potential conflict of interest between the two levels of government, particularly in setting priorities for programs into the budget.

The local own revenue is a potential source that is effective in promoting the performance of the budget. The mediator's role of grants and transfer, in fact, weaken the significant of local own revenue to the budget performance. This is because regions fiscal capacity is concentrated merely on the grants and subsidy, but effective financial management is on the local own revenue.

6. Limitation of the Study

Limitations of this study are first, samples are only from the district local government, while the overall local governments consist of provinces, cities, and districts. Second, the type of regional autonomy for the province, and district and city is different. Therefore, future research is expected to broaden the scope of research and to enrich the understanding of the behavior of local budgets at different levels of autonomy.

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Exhibit 1
Validity and Reliability Test for the Data.

No	Variables	Cronbach's Alpha	KMO	Variance Explained (%)
1	Local Revenues Own	0.971	0.853	93.354
2	Grants and Transfers	0.967	0.853	94.844
3	Budget Performance	0.957	0.839	90.995

Exhibit 2
Coefficients(a)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	10.4298	0.1851		56,337	0.00**)		
	Local Own Revenue	0.2706	0.0193	0.7133	14028	0.00**)	1.000	1.000
	a Dependent Variable: Budget Performance							
1	(Constant)	9.2529	0.211		43.909	0.00**)		
	Grant and Transfer	0.3281	0.022	0.735	14.921	0.00**)	1.000	1.000
	a Dependent Variable: Local Own Revenue							
1	(Constant)	3.4550	0.321		10.770	0.00**)		
	Grants and Transfers	0.772	0.026	0.908	29.815	0.00**)	1.000	1.000
	a Dependent Variable: Budget Performance							
1	(Constant)	10.430	0.185		56.337	0.00**)		
	Local Own Revenues	0.271	0.019	0.713	14.028	0.00**)	1.000	1.000
	a Dependent Variable: Budget Performance							
2	(Constant)	3.8713	0.366		10.573	0.00**)		
	Local Own Revenues	0.038	0.017	0.101	2.278	0.02*)	0.460	2.172
	Grants and Transfers	0.709	0.038	0.833	18.780	0.00**)	0.460	2.172
a Dependent Variable: Budget Performance								

**) significant at $\alpha = 0.001$, *) significant at $\alpha = 0.05$

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Exhibit 3 ANOVA(b)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	15.0796	1	15.0796	196.7954	0.00**)
	Residual	14.5589	190	0.0766		
	Total	29.6386	191			
a Predictors: (Constant), Local Own Revenue						
b Dependent Variable: Budget Performance						
1	Regression	22.101	1	22.101	222.642	0.00**)
	Residual	18.861	190	0.099		
	Total	40.962	191			
a Predictors: (Constant), Local Own Revenue						
b Dependent Variable: Grant and Transfer						
1	Regression	24.419	1	24.419	888.954	0.00**)
	Residual	5.219	190	0.027		
	Total	29.639	191			
a Predictors: (Constant), Grants and Transfers						
b Dependent Variable: Budget Performance						
1	Regression	15.080	1	15.080	196.795	0.00**)
	Residual	14.559	190	0.077		
	Total	29.639	191			
2	Regression	24.559	2	12.279	456.875	0.00**)
	Residual	5.080	189	0.027		
	Total	29.639	191			
a Predictors: (Constant), Local Own Revenues						
b Predictors: (Constant), Local Own Revenues, Grants and Transfers						
c Dependent Variable: Budget Performance						

**) significant at $\alpha = 0.001$, *) significant at $\alpha = 0.05$

Exhibit 4:

Test for mediator effect used Sobel Test:

$$\text{Sobel} = \frac{a * b}{\sqrt{(a^2 s_b + b^2 s_a)}}$$

$$a = 0.328 \quad S_a = 0.022$$

$$b = 0.2706 \quad S_b = 0.0193$$

$$\text{Sobel} = 14.2458, \quad p = 0.00$$

Where:

a = regression coefficient of Local Revenue

S_a = standard error of regression coefficient of Local Revenue

b = regression coefficient of Grant and Transfer

S_b = standard error of regression coefficient of Grant and Transfer