

## ICSSAM-1442

# **The Influence of Growth Capital Expenditures and Fiscal Stress on the Growth of Local Taxes (Research on District/City in West Java Province)**

**Diana Sari** \*

Widyatama University, Indonesia  
diana\_sari570@yahoo.com

**Karhi Nisjar Sardjudin**

Widyatama University, Cikutra Indonesia  
karhi@widyatama.ac.id

**Mailinda Utami Anandhari**

Widyatama University, Indonesia  
mailinda.utami@widyatama.ac.id

### **Abstract**

Availability of resources and readiness of potential areas is an important factor in the success of the regional autonomy era, but the availability of resources and the readiness potential in every area of the region is uneven causing fiscal stress. High fiscal stress reflects the regional effort to increase local taxes to reduce dependence on the central government level. Along with it, hopes to continue to improve its own admission it will be difficult to materialize when the allocation for capital expenditure is not increased because many more investors who want to invest in an area that has fulfilled its facilities.

This research is intended to know the influence of growth capital expenditures and fiscal stress on the growth of local taxes. The study was conducted at the district/city in West Java province in 2008-2011 with a sample of 25 districts/ cities. The method used is the method explanatory. Statistical testing using multiple linear regression analysis, where the effect of partial tested using t-test and simultaneous effects were tested using F-test. The results of this study indicate that partial, significant capital spending growth and have a negatif relationship to the growth of local tax and fiscal stress significantly and positively related to the growth of local taxes. Simultaneously, growth capital expenditures and fiscal stress significantly and positively related to the growth of local taxes.

**Keywords:** Growth Capital Expenditure, Fiscal Stress, and Growth of Local Tax.

## 1. Introduction

### 1.1 Research Background

Management of local governments changed with the enactment of Law No. 32 Year 2004 on Regional Government and Law No. 33 Year 2004 on Financial Balance between Central and Local Government are set on regional autonomy and fiscal decentralization. Consequences of the implementation of these laws is the area to be able to develop a broad regional autonomy, real, and responsible to improve services and welfare in a democratic society, fair, equitable, and sustainable. Obligation to improve services and public welfare can be met if the local government is able to manage the potential of the region, namely the potential of natural resources, human resources, and potential financial resources optimally (Sihite, 2010).

Regional autonomy policy provides an opportunity and a challenge for regional progress. Chances are areas can maximize the resources at their disposal to realize the independence of the region. According to Halim (2007: 17) regional autonomy policy challenges to the region to manage its resources effectively and efficiently in accordance with the generating capacity of each region, the result appears different fiscal readiness between one region to another.

High fiscal stress can influence the growth of local taxes, because according Shamsub and Akoto (2004) when the government is running high fiscal stress, the government tends to explore the potential tax revenue to increase income. High fiscal stress indicates the higher regional efforts to increase local taxes in order to reduce the level of dependence on central government. Along with it, hope to continue to improve its own admission it will be difficult to materialize when the allocation of expenditure for capital/development can not be increased because many investors prefer to invest in an area that has fulfilled its facilities, due to various considerations.

Table 1 describes the phenomenon that occurs in the District/City in West Java province that increased capital expenditure growth and high fiscal stress does not give effect to the increased growth of local taxes. The decline in the growth of local tax because the tax paying public awareness in the district/city in West Java province remains low even though the government has sought to provide a wide range of support facilities to increase income in the community. The increase in capital expenditures were higher still largely funded by the central government. Local governments must be able to achieve self-sufficiency regions with existing fund all expenses of the region's revenue itself.

Low levels of independence and still very dependent on the central government with a high capital expenditure growth and the policy of local autonomy and local tax collection restrictions will result in high stress for the fiscal area.

Fiscal high stress should be able to give effect to the average growth of local taxes, because of fiscal stress can be used as a tool to motivate the region in improving regional tax revenues.

Table 1: Growth Capital Expenditures, Fiscal Stress and Growth of Local Taxes in West Java province years 2008-2011

Year	Growth Capital Expenditures	Fiscal Stress	Growth of Local Taxes
2008	0,80%	0,0015	3,65%
2009	-5,74%	0,0017	30,69%
2010	22,53%	0,0019	25,56%
2011	31,13%	0,0019	16,55%

Source: Central Bureau of Statistics (BPS) of West Java province, data is reprocessed.

## 1.2 Identification of Problems

Based on the description of the background, the researchers identified the problem as follows:

1. How much influence of growth of capital expenditure on the growth of local tax district/ city in West Java Province
2. How much influence of fiscal stress on the growth of local tax district/city in West Java Province
3. How much influence of growth of capital expenditure and fiscal stress on the growth of local tax district/city in West Java Province

## 2. Literature Review

### 2.1 Capital Expenditures

Fixed assets held as a result of capital expenditure is a major prerequisite in providing public services by local governments. To add fixed assets, local government has allocated capital expenditure budget in the budget revenue and expenditure (APBD). Capital expenditure is based on local needs for facilities and infrastructure, both for the convenience of the government and for public facilities.

Halim (2004: 72) argues that capital expenditure is expenditure that benefits are likely to exceed the budget year and will add assets or wealth area, and will further add to the regular budget for operational and maintenance costs.

Based on the Indonesian Government Regulation No. 8 Year 2006, April 3, 2006, on Financial Reporting and Performance of Government Agencies in Appendix I-A.5 Government Budget Realization Report district/city, which includes capital expenditures are: 1) Land; 2) Equipment and Machinery; 3) Building and Construction; 4) Roads, Irrigation and Networks; 5) Other Fixed Assets; and 6) Other Assets.

## **2.2 Fiscal Stress**

Fiscal stress is the inability of a government to meet its budget (Halim, 2001). According to Chapman (1999) explains that fiscal stress occurs when the local government revenues decreased without compensation decline in demand for local government services, when people increase the demand for local government services and income can not be increased.

Bradbury in Chapman (1999) defines fiscal stress as a budgetary fiscal stress or citizen fiscal stress. Budgetary fiscal stress occurs when the local government can not balance the annual budget, the current account deficit is larger, the increasing financial pressure. Citizen fiscal stress occurs when people face an increased tax burden on the average level of local services are provided or when the level and quality of services decreased to an average tax burden.

According Setyawan (2008) with a high fiscal stress indicators do not reflect the efforts of the tax the following two things:

1. The district/city greater efforts to optimize revenue potential areas owned, so the tax revenue to be larger.
2. The area is more moderate in setting the revenue budget. If the tax effort be an indicator to determine the level of success (performance) area, the local government may be relatively more cautious in setting the budget.

## **2.3 Local Taxes**

Local tax is one component of revenue (PAD) with the most potential for development and is a source of local revenue. With the autonomy, the area can be driven to dig seek source of revenue derived from the tax sector that can support the financing of local expenditure.

According Siahaan (2010:10) states that the local tax is a tax set by local governments with local regulations, which authorized the collection held by the local government and the results are used to finance expenditures of local governments in implementing governance and development areas.

## **2.4 Hypothesis**

The hypothesis in this study are:

### **1. Partial**

Ho1: Growth capital expenditures are not positive and significant effect on the growth of local taxes district/city in the province of West Java.

Ha1: Growth capital expenditures are positive and significant effect on the growth of local taxes district/city in the province of West Java.

Ho2: Fiscal stress is not positive and significant effect on the growth of local taxes district/city in the province of West Java.

Ha2: Fiscal stress is positive and significant effect on the growth of local taxes district/city in the province of West Java.

## 2. Simultaneously

Ho3: Growth capital expenditures and fiscal stress are not positive and significant effect on the growth of local taxes district/city in the province of West Java.

Ha3: Growth capital expenditures and fiscal stress are positive and significant effect on the growth of local taxes district city in the province of West Java.

## 3. Methodology

The object of this research is capital expenditure, fiscal stress and local taxes are reported in the realization of the Budget (APBD) and Gross Regional Domestic Product (GDP) district/city in West Java province in 2008-2011.

The population in this study were all district/city in West Java province, amounting to 26 districts/cities. To determine the sample to be used in this study, the researchers will use purposive sampling technique. Based on these techniques, the selected sample is as much as 25 districts/cities in West Java province is composed of 16 districts and 9 cities. The method used in this research is explanatory.

The variables used in this study are:

### 1. Independent Variable (X)

Measurement of variables for growth capital expenditures (X1):

$$PBM = \frac{BM_t - BM_{t-1}}{BM_{t-1}} \times 100\%$$

(Source: Halim, 2004: 234)

Specification:

PBM = Growth capital expenditure

BM<sub>t</sub> = Actual capital expenditure given year

BM<sub>(t - 1)</sub> = Actual capital expenditure previous year

Measurement of variables to fiscal stress (X2):

$$\text{Tax Effort} = \frac{\text{Realization of Local Tax}}{\text{GDP}}$$

(Source : Halim, 2004:92)

Keterangan:

GDP = Gross Domestic Income

2. Dependent Variable (Y)

Measurement of variables for the growth of local tax (Y):

$$PPD = \frac{PD_t - PD_{t-1}}{PD_{t-1}} \times 100\%$$

(Source : Halim, 2004:234)

Keterangan:

PPD = Growth of Local Taxes

$PD_t$  = Realization of Local Taxes at given year

$PD_{t-1}$  = Realization of Local Taxes at previous year

Data analysis methods used in this research is multiple linear regression analysis as follows:

$$Y = a + b_1 X_1 + b_2 X_2 + e$$

Specification:

Y : The growth of a Local Taxes a: Constants

X1: Growth BelanjaModal b: Regression coefficient of the independent variable

X2: Fiscal Stress e: Error term

## 4. Results and Discussion

### 4.1 Effect on Growth Growth Capital Expenditures Local Taxes

Improved service to the community can be improved if the income is owned by the local government is also adequate. Although local governments get funding from the central government but also local governments should still be able to optimize the potential of the region in order to increase local taxes. With increasing local taxes such an area would be an area that is independent in accordance with the objectives of regional autonomy.

After testing the t test with a level signifikansi  $\alpha = 5\%$ , showed that capital spending growth has a negative and significant effect on the growth of local taxes.

These results are supported by research Adi and David Hariyanto (2007) which states that the capital expenditure and significant negative effect on the change in revenue (PAD). The relationship between growth capital expenditure (X1) with the growth of local taxes (Y) identified by the beta coefficient of -0.174. The coefficient is negative this means that the growth of capital expenditure with the growth of local taxes are the opposite relationship of 0.174. Therefore, when the growth of capital expenditure increase one unit, then the growth of local taxes will decrease by 0.174.

When viewed from the descriptive statistics as well as data growth capital expenditures and local taxes growth data in 2008-2011 can be concluded that the average growth of capital expenditure increased sharply each year in contrast to the growth of local taxes that have an average growth each year tends to decline. This is why the relationship capital spending has a negative effect on the growth of local taxes. The increase in capital spending growth is given by the government in the form of public service or in the form of infrastructure is not able to increase the growth of local taxes because the level of awareness of the taxpayer to pay taxes in the district/city in West Java province remains low even though the government has sought to provide a useful facility to increase incomes.

So this indicates that the average growth of local taxes decreased in the district/city in West Java province in finance capital expenditure growth is still dependent on central government funding, which should help the fund can be reduced in order to implement the independence of a region in order to support decentralization. The degree of independence of the district/city in the province of West Java can be said to have a low self-reliance that can be seen from the government financing is still very dependent on the central government to finance development spending.

#### **4.2 Fiscal Effect of Stress on Growth of Local Taxes**

After implemented regional autonomy, the government in under pressure greater than ever. This is because after the regional autonomy, government is expected to be more independent. One indicator of independence is the optimization of the growth of local taxes. But the local government not gets easy challenge, especially for district/city that have small fiscal conditions and resources.

District/city that have a low fiscal conditions and resources, tend to have a higher fiscal stress as compared to other district/city that have high fiscal conditions and resource. Therefore, to meet the demands of independence and improve their fiscal condition, district/city tends to further enhance the growth of local taxes.

This phenomenon supports research that shows that fiscal stress has positive and significant effect on the growth of local taxes. The greater the fiscal stress of a district/city, the greater the rate of growth in the district/city of local taxes. This can be seen from the test t test with a level signifikansi  $\alpha = 5\%$ , shows that the fiscal stress has a positive and significant impact on the growth of local taxes.

These results are supported by Setyawan (2008) which revealed that there is a positive and significant effect on growth of fiscal stress (PAD). According to Setyawan, (2008) with a high fiscal stress indicators do not reflect the efforts of the tax the following two things:

1. The district/city greater efforts to optimize revenue potential areas owned, so the tax revenue to be larger.
2. The district/city are more moderate in setting the revenue budget. If the tax effort be an indicator to determine the level of success (performance) district/city, the local government may be relatively more cautious in setting the budget. The budget process will be more integrated, rely on the participation of the staff of departments or agencies.

The relationship between fiscal stress (X2) with the growth of local taxes (Y) identified by the beta coefficient of 84.891%. The coefficient is positive that this could mean that the fiscal stress to local tax growth there is a direct relationship of 84.891. Therefore, when fiscal stress increase one unit, then the growth of local tax will rise by 84.891. This positive relationship indicates that the higher the fiscal stress, the higher the growth of local taxes.

When viewed from the descriptive statistics of fiscal stress and growth of local taxes in the year 2008-2011 can be concluded that the average fiscal stress increased sharply each year with growth of local taxes that have an average growth each year tends to decline. Supposed to be in the presence of high fiscal stress government must be motivated to increase local tax revenue but low public obligation to pay taxes can lead to low growth in local taxes annually.

It can be concluded district/city in the province of West Java has a weak level of independence that this indicated that the government district/city in West Java province is not motivated to increase tax revenues rise in the region because the government district/city in West Java Province prefers to rely on government funding center as funds for household purposes.

#### **4.3 Effect of Growth Capital Expenditure and Fiscal Stress to Growth of Local Taxes**

Fiscal stress levels increasing after autonomy tends to increase the growth of local taxes. Increased growth of local taxes provide opportunities ever greater allocation of funds for

capital expenditure. This is consistent with a recent study states that the variable capital expenditure growth and fiscal stress simultaneously significant effect on growth variables local taxes. This can be seen from the test f test with significance level  $\alpha = 5\%$ , shows that the growth of capital expenditure and fiscal stress simultaneously have influence positive and significant impact on the growth of local taxes.

This research was supported by research Wijaya (2012) which stated capital expenditure and fiscal stress simultaneously affect the increase in revenue (PAD) in the government district/city in North Sumatra. When viewed from the growth of capital expenditure, fiscal stress and growth of local taxes in the year 2008-2011 can be concluded that the high average of growth capital expenditure and the high average of fiscal stress on the district/city in West Java province have not been able to increase the average of growth local taxes annually. It is generated from community factors that do not have the desire and willingness to pay taxes and the government of factors that do not seek to increase the potential of the area and prefer to rely on equalization funds from the central government. Effect of growth capital expenditures and fiscal stress on the growth of local tax has the effect of 11% and the remaining 89% is explained by other factors that affect the growth of local taxes are not investigated and are not included in this study.

## **5. Conclusion**

Based on the analysis of the results of research and discussion, along with supporting theories, it can be concluded as follows:

1. Growth in capital spending has a negative and significant effect on the growth of local tax district/city in the province of West Java. If the amount of the higher capital expenditure growth, the lower the growth of local taxes.
2. Fiscal stress has a positive and significant effect on the growth of local tax district/city in the province of West Java. If greater financial pressures or fiscal stress of a district/city, the greater the rate of growth in the district/city of local taxes.
3. Growth capital expenditures and fiscal stress positive and significant effect on the growth of local taxes district/city in the province of West Java. If the capital expenditure and increasing fiscal stress will increase the growth of local taxes. Fiscal stress has increased after the autonomy tends to increase the growth of local taxes. Increased growth of local taxes provide opportunities ever greater allocation of funds for capital expenditure.

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