

## Conference Paper

# The Impact of the Original Local Government Revenue and Balanced Budget toward Capital Expenditure of the Government of Palangka Raya City

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### Abstract

The implementation of fiscal decentralization in improving services and necessity in various sectors including public sector has lead the Regional Government to allocate higher Capital Expenditure for the development of sectors that are considered beneficial in each region. The purpose of this study is that the researcher would like to investigate the impact of Original Local Government Revenue and Balanced Budget toward the Capital Expenditure of Palangka Raya City. The study was conducted in Palangka Raya City using a quantitative descriptive approach and multiple analysis for the data analysis. The results of the study indicates that part of Original Local Government Revenue does not have significant effect on Capital Expenditure. Meanwhile, part of the Balanced Budget has a significant effect on Capital Expenditure. Simultaneously, both of Original Local Government Revenue and Balanced Budget are able to influence local Capital Expenditure of the government of Palangka Raya City.

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Received: 7 February 2020

Accepted: 9 March 2020

Published: 23 March 2020

Publishing services provided by  
**Knowledge E**

**Keywords:** Original Local Government Revenue, Balanced Budget and Capital Expenditure

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Selection and Peer-review under the responsibility of the ICE-BEES 2019 Conference Committee.

## 1. Introduction

According to Law Number 32 Year 2004 about Regional Government and Law Number 33 Year 2004 about Balanced Budget of Central and Regional Government have turned out as an opportunity for districts and cities in Indonesia to manage their own budget (Law Number 32, 2004; Law Number 33, 2004). The regional autonomy policy has allowed provinces, districts and cities as economic centre areas. The provision of this policy makes both of the provincial and district/city governments are able to plan, explore, manage and use the regional budget that suit conditions of the area (Halim, 2016). Therefore, the regional government is expected to implement programs and

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activities that serve the citizen in all public services areas, such as health, infrastructure, education, etc.

Regional governments can improve public services by using a policy instrument known as the Revenue and Expenditure. Law Number 32 Year 2004 Article 1 (17) states that the Revenue and Expenditure is an annual financial plan of the regional government that has been discussed and agreed upon by both of the regional government and regional legislative assembly and imposed by regional regulations. The Revenue and Expenditure is the basis of regional financial management which is a guideline for local governments to provide services for the citizen within a yearly budget. the Revenue and Expenditure consists of regional income, regional expenditure, and regional financing

Regional expenditure consists of direct and indirect expenditure (Regulation of Domestic Affairs Minister Number 25 Year 2009). Regional Expenditure is the allocation of funds that must be spent effectively and efficiently as a benchmark for the success of regional autonomy. Within the regional expenditure account there is a Capital Expenditure account that is used to provide public services. Capital Expenditure is one of the concrete steps in improving public services from the regional governments, by allocating a number of funds in the form of a Capital Expenditure budget in the regional expenditure budget in order to add fixed assets. Capital Expenditure is allocated according to regional needs for facilities and infrastructure in order to support the implementation of government activities and public facilities. (Tsani, 2018) states that the greater the regional income obtained by districts/cities, the greater the allocation of Capital Expenditure to districts/cities in East Java Province. This is also supported by a research conducted by Sularno (2013) which states that Local Gross Domestic Product, Original Local Government Revenue, and General Allocation Fund, simultaneously influence the allocation of Capital Expenditures.

Original Local Government Revenue is a financing source completely originates from the local area. It usually consists of local taxes, regional levies, separated wealth management and other income. If the regional government has a large amount of Original Local Government Revenue, then the funds owned by the local government to finance Capital Expenditure are even greater. The increase in Original Local Government Revenue is expected to be one of the factors to overcome the problem of financing in the region and minimize the source of funding that comes from central government transfers.

Indonesia has a problem in terms of regional potential that is vary among islands, provinces, even among districts/cities that cause the regional government allocates a number of funds to overcome this problem through central government fund transfers

originating from the State Budget. This Balanced Budget consists of Revenue Sharing Fund, General Allocation Fund, and Special Allocation Fund. This Balanced Budget has a very large proportion, therefore, it becomes the main funding source for local governments.

Budget distribution variables emerges because of notions occurring in the field that budget distribution such as central government Balanced Budget is often misdirected and tends to be used to finance routine spending that are less productive (Asyaidah, 2015). This is also supported by a study on legislative opportunistic behavior in regional budgeting which states that political pressure in government can cause a distortion of budget utilization in projects that will be funded by the government budget (Abdullah & Asmara, 2006).

## 2. Literature Review

### 2.1. States Finances

The definition of state finance as contained in the explanation of article 1 paragraph 1 of Act Number 17 of 2003 concerning State Finance, is all state rights and obligations that can be valued with money, as well as everything in the form of money or in the form of goods that can be owned by the state in connection with implementation of rights and obligations. State Finance is managed in an orderly manner, complies with laws and regulations, is efficient, economical, effective, transparent and responsible by paying attention to a sense of justice and propriety.

Management of state finances is part of the implementation of state governance. Management of state finances is the overall activities of state financial management officials in accordance with their position and authority, which includes;

1. state financial planning;
2. implementation of state finances;
3. supervision of state finances; and
4. State financial accountability.

### 2.2. Regional Finance

The definition of regional finance as contained in the explanation of article 156 paragraph 1 of Act Number 32 of 2004 concerning Regional Government, is as follows: "Regional finance is all regional rights and obligations that can be valued with money

and everything in the form of money and goods that can be made belongs to the region related to the implementation of these rights and obligations ”

According to Halim (2007), the scope of regional finance consists of ”regional finances managed directly and separated regional assets. Included in regional finance that is managed directly is the Regional Revenue and Expenditure Budget and inventory items belonging to the region. ”Regional finance in the narrow sense is limited to matters relating to the Regional Revenue and Expenditure Budget. Therefore, regional finance is identical to the Regional Budget and Expenditure ”.

Theoretically, the government budget has three main functions as follows: the function of allocation, distribution and stability. As in allocation function, the budget plays a role in allocating public interests or administering the government in the interest of public services. As in distribution function, an equal distribution of income and eradication of poverty are served. While the function of stability is creating a conducive macroeconomic environment (Pratolo & Riyadi, 2007).

Financial balance between the Central Government and Regional Government is a fair, proportional, democratic, transparent and efficient financial distribution system in the frame work of funding the implementation of decentralization, taking into account the potential, conditions and needs of the region, as well as the amount of funding for Deconcentration and Co -Administration. Halim (2007) revealed that the ability of the Regional Government in managing regional finance is contained in the Regional Budget which is direct or indirect. Local Government Budget is the government’s main instrument for improving the welfare of its people and at the same time as a government’s instrument for managing the regional economy. For this reason, local government’s instrument need sufficient fund out their functions (Uhunwuangho&Aibieyi,2013)

### 2.3. Capital Expenditure

Capital Expenditure is an expenditure whose benefits tend to exceed one year and it increases the assets or wealth of the government, moreover, it will add to the routine budget for operational costs and maintenance costs (Nuarisa, 2013). Capital Expenditure is investment in the form of procurement or purchase of assets of more than 12 (twelve) months and those assets are used in government activities that are beneficial in economic, social, etc. Therefore, the government’s ability to serve community is improving (Halim, 2008).

## 2.4. Original Local Government Revenue

According to Law number 33 Year 2004, Original Local Government Revenue is a source of revenue explored in the local area to be used as the capital foundation of regional governments in financing development and regional businesses in order to minimize dependence on funds provided by the central government. Original Local Government Revenue is the right of the regional government which is recognized as a deduction of net worth within the fiscal year period. Sources of local revenue are the returns of regional taxes, regional retributions, separated regional wealth management, and other legitimate sources (Abdullah & Halim, 2003).

## 2.5. General Allocation Fund

General Allocation Fund is one of central government Balanced Budget to regional government originating from the State Budget which is allocated for equal distribution of financial capacity among regions in order to fund regional expenditure necessity as a form of decentralization implementation (Nuarisa, 2013). According to Law No. 33 year 2004, General Allocation Fund is a fund originating from State Expenditure Budget revenues which is allocated for equal distribution of financial capacity among regions in order to fund regional necessity as a form of decentralization implementation.

## 2.6. Special Allocation Fund

Special Allocation Fund is a fund originating from the State Budget allocated in certain regions with the aim to support special activities which belong to Local affairs in accordance with national priorities. Based on Regional Affairs Ministry Regulations number 33 year 2007, the use of Special Allocation Fund allocated to certain regions is to fund physical needs, basic facilities and infrastructure which belong to local affairs that include programs and activities of education, health, and so forth that following the technical guidelines imposed by related ministry based on the laws and regulations.

### 2.6.1. Relationship between Original Local Government Revenue and Capital Expenditure

One of regional government main tasks is to carry out development in its area in the form of infrastructure development in order to provide public services for its citizen.

One of the development efforts can be seen from the size of Capital Expenditure allocated to the regional government (Tsani, 2018). Local Own-Sources Revenue is an income originating from the local sources. If the Local Own-Sources Revenue increases, then Capital Expenditure will increase as well. Optimizing the Original Local Government Revenue should be supported by local government's efforts to improve the quality of public services (Mardiasmo, 2002). According to Ni Luh Dina Selvia Martini, Wayan Cipta, I Wayan Suwendra (2014) in a study entitled The Impact of Original Local Government Revenue, General Allocation Fund and Special Allocation Fund toward Capital Expenditure in Buleleng Regency in 2006-2012, the Original Local Government Revenue has an effect on Capital Expenditure.

### **2.6.2. Relationship between Budget Distribution and Capital Expenditure**

Budget distribution variables arise because there is a notion that the realization of budget distribution such as central government Balanced Budget is often misdirected and tends to be used to finance routine spending that are less productive (Asyaidah, 2015). Sheila Ardhian Nuarisa (2013) in her study entitled The Effect of Original Local Government Revenue, General Allocation Fund, Special Allocation Fund on the Allocation of Capital Expenditure Budget stated that the General Allocation Fund / Special Allocation Fund variable influences Capital Expenditure and has a positive coefficient direction. The researchers assumed that if General Allocation Fund and Special Allocation Fund increased, Capital Expenditure would increase as well.

### **2.6.3. Relationship of Original Local Government Revenue, General Allocation Fund, Special Allocation Fund, Budget Distribution toward Capital Expenditures**

The researcher assumed that if Original Local Government Revenue, General Allocation Fund and Special Allocation Fund increased simultaneously, the Capital Expenditures would increase as well. Darwanto and Yulia Yustikasari (2007) investigated the Effect of Economic Growth, General Allocation Fund, and Special Allocation Fund on the Allocation of Capital Expenditure. The results of the study indicated that the Original Local Government Revenue, General Allocation Fund and Special Allocation Fund variables had a positive and significant effect on the allocation of Capital Expenditure budget.

### 3. Research Method

This research is a quantitative study using secondary data. The researcher analyzed the influence of Original Local Government Revenue and Balanced Budget (General Allocation Fund / Special Allocation) on Capital Expenditures in Palangka Raya City. Data on Original Local Government Revenue, General Allocation Fund, Special Allocation, and Capital Expenditure are city-based data obtained from Central Bureau of Statistics of Palangka Raya City for 2013-2017.

The research variables are Original Local Government Revenue, Balanced Budget (General Allocation Fund / Special Allocation Fund) as independent variables and Capital Expenditures as dependent variables.

The researcher used descriptive statistical data analysis. Descriptive statistic is a statistic used to analyze data by describing or depicting them that has been collected without intending to make general conclusions or generalizations.

The research model used is a multiple linear regression analysis model which includes test of significance of individual parameters (t test), simultaneous significance test (F test) and coefficient of determination (R<sup>2</sup>).

### 4. Result of the Study

#### 4.1. Multiple Linear Regression Test (Hypothesis Test)

Multiple linear test analysis is done to test the research hypothesis whether there is any influence between variables X and Y or not. Variable X is the independent variable, whereas the variable Y is the dependent variable. The X variable in this study is Original Local Government Revenue and Fiscal Balance Transfer Fund (General Allocation Fund / Special Allocation Fund). While variable Y is Capital Expenditure of the Government of Palangka Raya City. The hypothesis of this study are as follows:

H1: Original Local Government Revenue has influenced the Capital Expenditure of the government of Palangka Raya City

H2: Balanced Budget have influenced the Capital Expenditure of the government of Palangka Raya city

H3: Both of Original Local Government Revenue and Balanced Budget have influenced the Capital Expenditure of the government of Palangka Raya city. The results of the study are as follows:

TABLE 1: Analysis Result of the Effect of Original Local Government Revenue and Balanced Budget on Capital Expenditures

Equation: $Y = 20006,8 + 0,250X_1 + 0,277X_2 + \epsilon t$		
t count:	0,957	(6,752)*
F count: (93,954)*		
R <sup>2</sup> : 0,998		

Note: \*)  $\alpha$  significant = 5% Source: SPSS output

### 4.2. T test

The t test is known as a partial test, it is used to find out how each independent variable influence the dependent variable. This test can be done by comparing t count with t table or by looking at the significance column in each t count.

In accordance with table 1, it is shown that the local-own source variable (X1) has a t count value of 0.957, while the t table value is 2.57. So that Original Local Government Revenue (X1) has no effect on Capital Expenditures. It can be concluded that H1 is rejected.

Whereas for the Balanced Budget variable (X2) has a value of t count 6.752, while the value of the t table is 2. The value of t count is greater than t table (6.752 > 2.57). Because t count is greater than t table for Balanced Budget variable, it can be concluded that the Balanced Budget have effected the Capital Expenditure in the government of Palangka Raya city. It is concluded that H2 is accepted.

### 4.3. F test

From the ANOVA test results for the simultaneous test it is known that the significance value of the F value is 93.8, while the F table is 3.03. It indicates that the F count value is greater than the F table value (93.8 > 3.03). This shows that simultaneously Original Local Government Revenue and Balanced Budget variables have significantly influenced the Capital Expenditure.

### 4.4. Coefficient of Determination R2

From table 1 it is known the value of R<sup>2</sup> = 0.998, meaning that the variation in changes in the Capital Expenditure variable can be explained by variations in the Original Local Government Revenue and Balanced Budget variables of 99.8%, the rest are explained by other variables outside the model.



#### 4.5. Relationship between Original Local Government Revenue and Capital Expenditures

This result implies that there is inadequate evidence for Original Local Government Revenue in increasing regional Capital Expenditure, in other words, Original Local Government Revenue has a negative effect on Capital Expenditure. It is obvious that the Capital Expenditure of Palangka Raya city is increasing every year, however, the accumulation has not been able to increase significantly. It is known that the Original Local Government Revenue of Palangka Raya city only contributes 15% to the Local Government Budget, Original Local Government Revenue only depends on the service sector. Whereas other sources have not yet been found.

Capital Expenditure tends to require a substantial allocation of funds, therefore, low size of Original Local Government Revenue partially is not able to influence it. Other factors indicated to be the roots of Original Local Government Revenue has a negative effect on Capital Expenditure as a result of local governments tends to allocate Original Local Government Revenue to finance other expenditures such as personnel expenditure which is more urgent (personnel expenditure that could not be postponed) and also to finance routine expenditure / operational expenditure. This result does not match the results of study conducted by Ni Luh Dina Selvia Martini, Wayan Cipta, I Wayan Suwendra (2014) which affirmed that Original Local Government Revenue had an effect on Capital Expenditure.

#### 4.6. Relationship between Balanced Budget and Capital Expenditure

Based on multiple linear tests, it is detected that the Balanced Budget are capable to influence Capital Expenditure in the government of Palangka Raya City. This signifies that the connection between Balanced Budget and Capital Expenditures is adequately durable. Balanced Budget from the central to the local government in the form of General Allocation Funds and Special Allocation Funds are adept to provide a stimulus for Capital Expenditure in the form of infrastructure / physical. Balanced Budget also provide evidence of being able to make Capital Expenditure more dynamic thus there is a positive and significant influence. The Balanced Budget contributes almost 85% of Local Government Budget. Most of the regional expenditure in Palangka Raya city is funded by Balanced Budget as a result of the limited number of Original Local Government Revenue of Palangka Raya City. This is in line with the result of study conducted by Sheila Ardhian Nuarisa (2013) which stated that the General Allocation Fund / Special

Allocation Fund variable influenced Capital Expenditure and had a positive coefficient direction.

#### **4.7. Relationship among Original Local Government Revenue, Balanced Budget and Capital Expenditure**

The results of the F test or the combined test indicate that the Original Local Government Revenue and the Balanced Budget simultaneously are able to influence Capital Expenditure in the government of Palangka Raya City, Central Kalimantan. Original Local Government Revenue and Balanced Budget are increasing year by year, this will be able to boost regional Capital Expenditure. Local tax revenues are greater when compared to the regional levies revenues, this by reason of the sources of Local Retribution revenues have not been managed properly so the proportion of Local Retribution in Original Local Government Revenue is still small.

In this study General Allocation Fund does not redundantly contribute to Capital Expenditure as a result of the government in financing local development uses more of the Special Allocation Fund. There are specific rules for the use of Special Allocation Fund that have been set up primarily to be allocated to Capital Expenditure. General Allocation Fund is mostly used to finance direct expenditure, especially employee expenditure and other operational expenditure. This result is in line with the study conducted by Darwanto and Yulia Yustikasari (2007) which stated that Original Local Government Revenue, General Allocation Fund and Special Allocation Fund had a positive and significant effect on the allocation of Capital Expenditure budget.

### **5. Conclusion**

From the results of the study, it can be concluded

1) Part of Regional Original Local Government Revenue is not able to influence the Capital Expenditure of the government of Palangka Raya City in Central Kalimantan. This means that the proportion of Original Local Government Revenue still cannot contribute to regional Capital Expenditure.

2) Part of The Balanced Budget have an influence on Capital Expenditure. This happened because the Balanced Budget is able to increase the distribution of regional budgets, which had an impact on Capital Expenditure. With the increase in Fiscal Balance Transfer Fund, it will give a stimulus to Capital Expenditure.

3) Original Local Government Revenue and Balanced Budget can influence Capital Expenditure in the government of Palangka Raya City in Central Kalimantan simultaneously. This is supported by loads of evidence that Original Local Government Revenue and positive Balanced Budget will have an impact on increasing Capital Expenditure.

## 6. Suggestion

From the conclusions above, the researcher's suggestions are:

1) For the government of the Palangka Raya City, in order to be able to optimize local revenue so that the accumulation of regional Capital Expenditure will increase, Original Local Government Revenue sources must be well inventoried so that Original Local Government Revenue is able to increase every year. The regional government must also optimize the potential of taxes and levies thus the regional revenues can escalate, especially because of the Local Retribution of Palangka Raya city is still considered minuscule.

2) For other researchers to consider other variables related to regional Capital Expenditure. They can provide suggestion about the variables' analysis and decision as well.

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