

# THE PROBLEMATIC OF PROVINCIAL TAX COLLECTION AS LOCAL OWN-SOURCE REVENUE IN INDONESIA

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## ABSTRACT

*Regional autonomy granted on local government to regulate and administer the governmental affairs in order to improve the efficiency and effectiveness of public services. To do so, the local government is authorized to collect taxes from its people. This research aimed to investigate the problematic of provincial tax collection in order to increase the own-source revenue of autonomous areas in Indonesia. The collection of local taxes is still not optimal. Thus, some necessary actions for betterment need to conduct, such as: a). Improving the human resources of tax authorities in terms of their capability in planning and monitoring the collection of taxes; b) Using technology of information to provide a fast and efficient services; and c) Enforcing the law to each of the taxpayers who violate the regulation of provincial taxes.*

**Keywords:** Local Taxation, Local Own-Source Revenue, Province, Collection.

## INTRODUCTION

The correlation between central and local governments is stated in the third and fourth paragraphs of the preamble of the Constitution 1945. The third paragraph contains the Declaration of Independence of the Republic of Indonesia and the fourth paragraph contains the statement that after declaring their independence, the first organization held was the Government of Indonesia; the national government responsible to organize and take care of Indonesia as a country. Furthermore, it mentions that the responsibility of the Government of Indonesia is to protect the nation and the people of Indonesia, promote the general welfare, educate the life of the nation and maintain the world order based on the notion of independence, ever-lasting peace and social justice (Huda, 2017).

Article 1 of the Constitution 1945 mentions that Indonesia is a unitary country which is a republic. As the result, the central government should establish local governments as set forth in article 18 paragraph (2) and (5) of the Constitution 1945, stating that the local governments are authorized to regulate and manage their own governmental affairs based on the principles of autonomy; and for the additional tasks, they are autonomous as widely as possible. Article 10 Act No. 23/2014, on Local government, sets the authority of the central government and it includes: Foreign policy, defence, security, justice, national fiscal and monetary, as well as religion (Sutedi, 2008).

In order to organize the government of the Republic of Indonesia, it is classified into provincial areas which consist of districts and cities. Each of the areas has right and obligation to govern and manage their own governmental affairs in order to improve the efficiency and effectiveness in organizing the government and public services.

To organize a government, each local government is authorized to collect taxes toward its people. Both act No. 28/2009 on Local Taxes and article 2 subsection (1) on Local Retribution provide a provincial authority to collect 5 kinds of taxes, including motor vehicles, vehicle ownership title transfer fee, vehicle fuel tax, surface water tax and cigarette tax. Thus, the local governments, particularly the provincial one, may collect their financial sources in particular to meet the needs of their local budget.

Up to recent days, however, 34 provinces in Indonesia have not been able to optimize their potential of local taxes, which belong to their authority. Consequently, it resulted in the disharmony between financial sources and expenditure in their local budget. We could see this matter from three provinces with very-high ratio of total budget: DKI Jakarta 33.85%, Bengkulu 27.12% and Central Sulawesi 23.56% (Rahman, 2017). Looking into this result, it indicates that the provincial governments are not able yet to be autonomous in their management of budget, thus, they need an allocation of finance from the central government to organize their provincial governments. The following table presents the overall data of provincial budgets in last three years.

<b>Kinds of Revenue</b>	<b>2013</b>	<b>2014</b>	<b>2015*)</b>
<b>A. LOCAL REVENUE</b>	<b>205.780.279.058</b>	<b>233.277.408.354</b>	<b>264.056.789.650</b>
<b>1. Own-source revenue</b>	<b>101.596.400.437</b>	<b>121.450.818.035</b>	<b>136.355.998.144</b>
1.1. Local taxes	86.979.670.640	103.087.606.002	120.326.064.477
1.2. Local retribution	1.267.843.490	1.705.308.478	1.731.839.091
1.3. Revenue of Local owned businesses and separated-assets management	2.837.923.962	2.972.476.313	3.485.394.400
1.4. Other legal revenues	10.510.962.345	13.685.427.242	10.812.700.176
<b>2. Counter balance fund</b>	<b>64.834.193.347</b>	<b>68.882.788.511</b>	<b>73.294.422.494</b>
2.1. Profit sharing of taxes	17.781.418.940	17.481.607.781	21.500.061.188
2.2. Profit sharing of nontaxes/Natural resources	14.299.514.233	15.406.003.394	13.426.024.074
2.3. General allocation of fund	30.977.874.897	34.121.932.565	35.971.973.787
2.4. Specific allocation of fund	1.775.385.277	1.873.244.771	2.396.363.445
<b>3. Other legal revenues</b>	<b>39.349.685.274</b>	<b>42.943.801.808</b>	<b>54.406.369.012</b>
<b>B. Local Financing</b>	<b>31.556.200.366</b>	<b>28.435.496.655</b>	<b>23.661.436.136</b>
<b>Total Amount</b>	<b>237.336.479.424</b>	<b>261.712.905.009</b>	<b>287.718.225.786</b>

### **Management of Local Autonomy**

The Government of Indonesia has changed several times and of course, those changes were not naturally born. A variety of major events had appeared for the sake of those changes which might make Indonesia better. The system selection for this unitary country initially agreed on two models of governmental interconnectedness which may link the central government to the local ones. The first model was termed as centralization, which put all governmental affairs, functions and authorities into the central government with de-concentration on its

implementation. The second model was decentralization, which put all governmental affairs, functions and authorities into the local government.

Centralization is a governmental design positioning the central government as the sole stakeholders for Indonesia's development and thus, it makes the central government superior and leads the local government into inferior. The central government then makes the local areas as objects in which local changes are defined by the central government. This may reveal inequality of interconnectedness between central and local governments in terms of whether economy, politic, education or other sectors (Sjuhri, 2010).

As time goes by, the centralized system turned into decentralization due to reformation on Indonesia government as set in Act No. 22/1999, revised by Act No. 23/2014, about local government. The act of local government basically regulates the organizational system of local government that focuses on the implementation of decentralization. It is expected that the effect of this principle of decentralization may create an equitable and sustainable welfare for people as well as the rise of social participation for democratization.

According to Bolatito, the character of decentralization has five aspects including:

- Legal personality;
- Localness;
- Effective participation by citizens;
- Extensive budgetary an employing self-sufficiency in regard to bounded control from central authority and e. Particular powers to execute a variety of functions (2014).

A consequence of selecting decentralized system is that the financial linkage between central and local governments may occur. Thus, it needs a system to delegate the authority on financial sector between central and local governments (Lozina, 2008). This decentralized financial policy is expected to have certainty in gaining revenue from different sources, so that it is not solely dependable on the central government's financial sources; which may eliminate the existence of their own autonomy (Nasution, 2011).

Decentralization on financial management of local governments is also one fundamental aspect for local autonomy. To organize an actual and accountable regional autonomy, it needs authorities and capabilities to seek for its own financial sources backed by financial equilibrium between central and local governments and between provinces and districts/cities as the prerequisite of local governmental system. The financial linkage between central and local governments is a kind of interconnectedness among a wide range of central and regional interconnectedness, however, financial equilibrium is the most sensitive problem to be solved.

To carry out the obligation and implement its autonomy and as the part of distributing the organization of governmental authority, the local governments need adequate financial sources. To carrying out their autonomy, multiple financial sources are available to back up the implementation of autonomy. Those include local own-source revenue as financial sources for implementing the autonomy (UN-Habitat, 2015). However, it is apparent that due to the lack of reliable sources on each area in order to gain local own-source revenue, the implementation of regional autonomy has no implication toward the local government to cover all their financial needs with their own-source revenue. In this context, decentralization on financial sector is a solution for the central and local governments to utilize the financial sources obtained within the confines of Indonesia territory to be used and distributed in proportional and rational manner between the two governmental levels.

The existence of division on financial sources between central and local governments

implies the local governments to implement their autonomy by relying their financing not solely on local own-source revenue due to insufficient budget to cover all their autonomous tasks but also on financial sources transferred by the central government as part of the local governments' rights. Hence, the inception of this financial equilibrium policy indicates that regions are authorized to utilize their own financial sources autonomously and it will be supported by proportionate and fair financial equilibrium between the two levels of governments.

The act of regional autonomy mentions that financial equilibrium is divided into three parts, including profit sharing, general allocation of fund and specific allocation of fund. Profit sharing is divided into profit-sharing of property tax under a condition that the state's revenue from property tax will be divided with an equalization that 10% for central government and 90% for local government. The intended local fund is then divided into 16.2% for the pertinent province, 64.8% for pertinent region and 9% for collection fee. In addition, 6.5% of 10% fund of the central government is allocated throughout the districts for the sake of equalization and the remaining 3.5% is allocated to the regions which is capable to surpass the target. Furthermore, general allocation of fund is a kind of allocation by the central government to reveal fiscal equilibrium among each region or to avoid any inequality on economy between them. The annual budget of the central government requires 26% of the amount as general allocation to all provinces and cities/districts in Indonesia. The proportion is 90% for regions and 10% for provinces. The specific allocation of fund is the allocation of the central government's fund toward particular regions since they are the scale of priority for national development in various aspects of public services such as public health, defence, public order and security, economy, environment, housing and public facilities, culture and religion (Sjubahri, 2010).

According to Minassian (1997), the equilibrium on providing authority of taxes should consider the following notions:

- The tax is for economic stability and the distribution of revenue should remain on the central government's responsibility;
- The tax base assigned to the local governments should not be too much "mobile". A very "mobile" local tax may force the taxpayers to relocate their business from high-tax areas to low-tax area. Instead, the non-mobile tax base may make the regions easier to set different tax rates as a reflection of societal capacity. For this reason, many countries submitted the tax of consumption to the local governments due to the equilibrium of the quite extensive areas (e.g. province in Canada). Therefore, the "mobile" tax base is the main prerequisite for maintenance in higher governmental level.
- The tax base with lop-sided distribution between central and local government should be assigned to the central government;
- The local taxes should be visible, in the sense that it should be obvious for every local taxpayer. The object and subject of taxes along with its amount should be easily calculated in order to encourage the accountability of the local government;
- The local tax should be charged to other regions since it may weaken the relations between the taxpayers and the services they receive (tax is a function of service);
- The local tax should become the source of revenue sufficient to prevent any lameness of high vertical fiscal. Ideally, the revenue should be elastic over time and not too fluctuating;
- The tax collected to the local government should be relatively easy to administrate. In other word, it needs an efficient equilibrium in economy related to the needs of data such as identification of the number of taxpayers, law enforcement and computerization;
- Taxes and retributions, based on the principle of benefit, should be used properly in each of the governmental levels; however, the assignment of authority for tax collection toward the regions will be appropriate as long as the usage is allocated for the local taxpayers.

Article 2 subsection (1) Act of Local Taxation regulates the kinds of provincial taxes consisting of: a) Vehicle tax; b) Vehicle ownership title transfer fee; c) Vehicle fuel tax; d) Surface water tax; and e) Cigarette tax. These taxes are limitative, which means that provinces may not collect other taxes but the specified ones. The restriction of tax collection by the provinces associates with governmental authority as an autonomous region and it is applied across the local governments of cities and/or districts and with the authority on particular fields. The criteria of the local government authorized to set its own tax are as follow.

- It refers to tax, not retribution;
- The object of the tax is in the territory of the region;
- The object and the base of the tax is not against the common interest;
- The object of the tax is not the authority of the central or local governments; whether cities or districts;
- The potential revenue of the local tax is sufficient;
- It does not bring any negative impact on society, in terms of their economy;
- It considers the aspect of fairness and people capability; and
- It keeps the sustainability of the natural environment.

### **The Role of Provincial Tax in Increasing Local Own-Source Revenue**

The financial linkage between the central and local governments can be reviewed from the provision of Act mentioning some kinds of taxes and retributions to become local taxes and retributions. Commonly, the source of collected taxes and retributions has a base for collecting taxes and the object and subject of taxes and retributions is on and related to the region itself.

Assigning several kinds of taxes and retributions to the local government is based on a regulation established by the central government. It is Urgent Act No. 11/1957 on Local Taxation and Act No. 12/1957 on Regional Retribution and after so many decades and along with a series of amendments on Act of Local Government as the primary provision, Act No. 18/1997 on Local Taxation and Retribution in finally established in 1997. It was then amended by Act No. 22/1999, revised by Act No. 34/2000 about the amendment of the Act No. 18/1997 on Local Taxation and Retribution. Furthermore, the Act No. 32/2004 was then used after a series of amendments and finally the Act No. 28/2009 on Local Taxation and Retribution is currently used (Nasution, 2011).

The policy of tax collection by the provincial government is based on regional regulation and it is attempted not to bring any clash with the taxation by the central government (taxes and/or custom and excise) since it may cause a duplication of tax collection which leads to economic distortion. It has been actually anticipated by Act No. 18/1997 on Local Taxation and Retribution as amended by Act No. 34/2000, mentioning in article 2 subsection (4) that the object of local tax is not central tax (Akbar, 2011).

According to Sidik (2002), the principles of good local taxation should meet some general criteria of local taxation as follow.

- The principle of providing sufficient revenue and it should be elastic, indicating that the revenue can be easily up and down along with the fluctuation of people income;
- Fair and equitable in vertical fashion, indicating that it should correspond to the level of society and in horizontal fashion, indicating that it should be equal for every member of the society with no one is immune from taxation;
- Flexible administration, indicating that it should be simple, easily calculated, satisfying services for the

taxpayers;

- Politically acceptable by public, so that it may motivate them to pay taxes;
- Non-distortion on economy sector which may imply the tax or retribution and bring minor effect on economy. Basically, every tax or retribution may burden both the consumers and producers. However, it is expected that a tax or retribution will not reveal any excessive extra budget which may lead people into dead-weight loss.

However, Tran-Nam (2015) defined the criteria of good taxation into:

- Registration in the system;
- Timely filing or lodgement of requisite taxation information;
- Reporting of complete and accurate information (incorporating good record keeping); and
- Payment of taxation obligations on time”, since tax is an obligation to do particular amount of payment without having any reward (Radvan, 2017).

In order to uphold the principles, local taxation should have particular characteristics. The characteristics of taxation applied in some developing countries are as follow.

- Local taxes are economically collected, indicating that the revenue of taxes should be higher than its cost;
- Relatively stable, indicating that the revenue is sometimes drastically decreased; and
- The tax base should refer to a synthesis between the principle of benefit and the capability to pay tax (Sidik, 2002).

The large number of tax compensation depends on the interaction between the government and the taxpayers. The cause of tax compensation involves:

- Tax control, including the protection of budget;
- The application of tax regulation for non-political purposes;
- The expansion of sources of taxable income;
- The increasing number of taxpayers;
- The frequency of amendment in regulation of taxation;
- The moral of tax;
- The mentality of tax;
- The increasing inter-connectedness between global and domestic economy; and
- The aggressive taxation planning.

### **The Optimization of Local Tax Collection to Increase Local Revenue**

The main characteristic indicating that an autonomous region is able to be autonomous is on its financial capability. Autonomous regions should have authority and capability to seek for, manage and use their own financial sources to be sufficient for organizing their local government. The capability to seek for local own-source revenue should be improved in order to support the finance of provincial government. Therefore, it needs the intensification and extensification on the subject and object of taxes. Intensification by provincial government in the near future is utilizing the technology of information. Utilizing integrated technology of information for tax intensification is absolutely necessary since the system of tax collection implemented all this time is not yet optimal (Radvan, 2016).

It can be seen from the conventional system and procedures of collection and from the partial implementation of the system, so that it is likely to provide inaccurate information.

Hence, the utilization of technology of information is expected to bring quick and efficient services toward every taxpayer. In addition, it needs to increase the human resources on tax authorities by improving their capability in planning and monitoring the collection of taxes in order to reach the target of collection by year and thus, significantly increase the revenue of taxes, as well as the implementation of legal enforcement on taxpayers violating the provision of provincial taxation.

In order to optimize the local own-source revenue in Local Budget, provincial governments need to extend the subject and object of taxes as follow (Sidik, 2002):

- Expanding the basis of revenue. It points to the regions with economic potential, such as identifying the new subject of tax, the tax base, as well as the kinds of tax;
- Strengthening the process of collection. Provincial government makes efforts to strengthen the process of collection by accelerating the enactment of regional regulation, adjusting the rate of taxes and improving the human resources;
- Increasing the supervision/controlling by conducting periodical and sudden monitoring, improving the process of supervision on tax authorities and enhancing the tax services;
- Improving the efficiency of administration and pushing down the cost of collection. Provincial government needs to fix its administration of taxation by simplifying the tax administration and making each kind of tax collection efficient;
- Improving the capacity of revenue through better planning and by increasing coordination with relevant instances in the area.

## CONCLUSION

The provision of taxation is set in Article 23A The Constitution 1945 mentioning that taxes and other coercive retributions for national interests is set under regulations. The provision of this article is implemented by Act No. 28/2009 on Local Taxation and Retribution, especially on Article 2 subsection (1) that provides authority toward provincial governments to collect 5 (five) kinds of taxes including motor vehicles, vehicle ownership title transfer fee, vehicle fuel tax, surface water tax and cigarette tax.

Local tax is a component of financial sources for provincial governments in Local Budget. Up to recent days, provincial government has not been able to meet the needs of funding in provincial Budget derived from Local taxes. Provincial governments should be independent from the central government and they should be off from any financial equilibrium in order to have accountability on their financial management.

In order to increase the autonomy of provincial governments, it needs strategic actions to increase the local own-source revenue which may meet the budgetary needs for local development. The policy that provincial governments may implement is intensifying and extending the subject and object of taxes.

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