

**Level of Regional Financial Independence
in the Eastern Region of Indonesia: Regional Original Income, Employee
Expenditures and Capital Expenditures**

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Abstract

Regional financial independence is an indicator of a region's ability to carry out regional activities independently without depending on other parties. Regional financial independence is generally influenced by several factors. One factor of independence is Regional Original Income. This research aims to examine the influence of Regional Original Income, employee expenditure, and capital expenditure on the level of regional financial independence. The research method used is quantitative replication research with multiple linear regression analysis as the analysis method. The research sample was 65 consisting of 17 regions with 5 (five) years of observation. The research results show that local revenue and employee expenditure influence the level of regional financial independence, while capital expenditure does not have a significant influence on the level of regional financial independence.

Introduction

The success of regional autonomy cannot be separated from ability in the financial sector, which is an important indicator in facing regional autonomy. One of the government's goals in implementing regional autonomy is to provide freedom for regions to manage their households to increase development for community welfare (Adhim et al., 2023).

A general phenomenon regarding the level of regional financial independence faced by most regional governments in Indonesia is the high dependence of regional governments on the central government as seen from the relatively low role of PAD in the APBD structure (Sutrisno & Santoso, 2021). According to Qoriiba, Aswar, and Ermawati (2021), regional financial independence is the ability to carry out regional activities independently without depending on other parties.

Original regional income is one of the regional rights that is recognized as adding to the value of net assets (Koraag & Cahyaningtyas, 2020). Research from Kristina, Naukoko, and Siwu (2021) concludes that regional original income has a positive effect on the level of regional financial independence. This is in line with research from (Machfud et al., 2021).

Employee expenditure is all forms of government expenditure to fund compensation provided by the government as a *reward* for work that has been carried out in the form of money and commodities available to civil servants (Fitriyani & Suwarno, 2021). Research from Defitri (2020) states that employee spending does not affect the level of regional financial independence. This is supported by research from (Sefira & Budiwitjaksono, 2022).

According to Iriabije, Ettah, and Nwosu (2023), capital expenditure is money spent on investment goods in hospitals, schools, the electricity sector, telecommunications, and road construction. Research from Riyadi (2022) states that capital expenditure has a positive effect on the level of regional financial independence. This is in line with research from (Angelina et al., 2020).

This research used a sample of 65 observations from 13 regions in the Eastern Province for 5 (5) years. This research aims to test and analyze the influence of local revenue, capital expenditure, and employee expenditure on the level of regional financial independence. This research analyzes *65-panel data samples*. This research is structured to include the first part; introduction, second part; literature review, and hypothesis. The third section presents the research method. The fourth section explains the results and discussion. The final section summarizes the study conclusions.

Literature Review and Hypothesis

The theory of fiscal federalism or *fiscal federalism* considers fiscal relationships at the level of government, decentralization, services, and welfare in society. Fiscal decentralization policy is the transfer of central government authority and responsibility in the political and administrative fields to regional governments (Undang-Undang Nomor 1, 2022). *Stewardship* theory explains that the government is not motivated by individual interests but the main target results are aimed at the public interest (Saraswati & Nurharjanti, 2021).

Sefira and Budiwitjaksono (2022) state that regional financial independence is the ability of a region to finance all government activities and regional needs without being too dependent on transfers from the central government. It is also quoted (Bella, Sari, & Rahmi, 2022) that regional original income is a source of funding or income that needs to be explored for the potential of the region itself because it can reflect the actual regional conditions (Oktavianti et al., 2023).

According to Fitriyani and Suwarno (2021), employee spending is purchases used by the government to finance compensation given to employees in the form of salaries and allowances. Capital expenditure is defined as expenditure that provides benefits in the future, as there may be a lag between when it occurs and when it impacts the economy.

Hypothesis

The implementation of *Stewardship* is due to the good management of local revenue for the common good so that the region does not depend on other regional or central governments, even vice versa. Original regional income has an important role in regional financial independence because original regional income looks at the extent to which a region can finance government and development activities so that it can be said to be independent in its performance. This is in line with research from (Machfud et al., 2021).

The implementation of fiscal decentralization is due to the responsibility for managing employee expenditure, especially in calculating salaries properly. Defitri (2020) concludes that employee expenditure is a form of compensation in the form of salaries and allowances

paid to government employees, civil servants, and employees who are employed without civil servant status as compensation for work that has been carried out. This is supported by research from (Sefira & Budiwitjaksono, 2022).

The implementation of fiscal federalism is because if capital expenditure is not managed well, the government's efforts to provide services and public welfare will be hampered. Defitri (2020) concluded that capital expenditure is still uneven or low so there is a lot of inequality in the level of financial independence between regions. This is in line with research from (Angelina et al., 2020).

Based on the thoughts and results of previous research, the following hypothesis was formulated :

H₁: Regional Original Income Influences the Level of Regional Financial Independence

H₂: Employee Expenditures do not affect the Level of Regional Financial Independence

H₃: Capital Expenditures Influence the Level of Regional Financial Independence

Research Methods

This research aims to analyze the influence of local revenue, personnel expenditure, and capital expenditure on the level of regional independence using annual panel data for 2018-2022, which covers 13 regions out of 17 regions in Eastern Indonesia that meet the requirements. This period is sufficient to obtain a total of 65 observations. One of the advantages of panel data is that it has a larger number of observations and degrees of freedom. This approach avoids regression problems and offers a simpler panel data approach to a broader and more dynamic model structure. Regional original income, employee expenditure, and expenditure are collected and accessed via the website <https://djpk.kemenkeu.go.id/>. Sampling is based on regions whose data is available through the website of the Directorate General of Fiscal Balance.

The analysis method uses linear regression analysis with the help of *Eviews* version 12 software. This method is a method for predicting factors that influence the level of regional independence. Prediction of variables that influence the level of regional independence begins with statistical descriptions, regression model analysis, hypothesis testing, and regression model accuracy testing. The regression model used to test the hypotheses (H₁, H₂, and H₃) is as follows:

$$TKKD_{it} = \beta_0 + \beta_1 PAD_{it} + \beta_2 BP_{it} + \beta_3 BM_{it} + \varepsilon_{it} \quad (1)$$

TKKD is the level of regional independence. PAD is the realization of Regional Original Income, BP is the realization of employee expenditure, and BM is the realization of capital expenditure. Realization of PAD, realization of personnel expenditure, and realization of capital expenditure are collected from the budget realization report, while the level of regional independence is obtained from the ratio of results for Regional Original Income with transfer income and others. Meanwhile, hypothesis testing (H₁, H₂, and H₃) from observation data from 2018 to 2022 is panel data from 13 company years.

Results and Discussion

Description of Research Sample

The research sample used data from the Provincial Government in the Eastern Region and was selected based on conditions that met the sampling requirements with the following details:

Table 1. List of samples in Eastern Indonesia

No	Code	Province Name
1.	Papua	Papua Province
2.	PaBar	West Papua Province
3.	Maluku	Maluku Province
4.	MalUt	North Maluku Province
5.	Ignite	North Sulawesi Province
6.	GoTa	Gorontalo Province
7.	Central Sulawesi	Central Sulawesi Province
8.	West Sulawesi	West Sulawesi Province
9.	Southeast Sulawesi	Southeast Sulawesi Province
10.	South Sulawesi	South Sulawesi Province
11.	Bali	Bali province
12.	NTB	West Nusa Tenggara Province
13.	NTT	East Nusa Tenggara Province
Total Sample		13 Provinces

Source: DJPK Ministry of Finance, 2023

Table 1. describes the number of samples that meet the sample determination criteria from 17 regions and meet the requirements in 13 regions. The number of people who meet the criteria requirements is 13 Provincial Government regions during 2018-2022, so the number of samples that can be processed and analyzed is 65 observations.

Descriptive Statistics

Table 2 presents statistical descriptions of each variable.

Table 2. Descriptive Statistics

	TKKD	PAD	BP	BM
Mean	18.22140	14.01855	32.29538	18.86569
Median	13.04604	11.54046	34.30504	18.54310
Maximum	87.80079	46.75209	39.90440	26.74968
Minimum	3.998192	3.844483	16.24615	9.546132
Std. Dev.	17.95265	9.465081	5.845634	4.088549
Skewness	2.876527	2.177360	-1.392446	0.110805
Kurtosis	10.93641	7.718624	3.861353	2.395853

Source: Results from Eviews 12, 2023

TKKD with a maximum of 87.80, a minimum of 4.00, a standard deviation of 17.95, and a mean of 18.22 proves that the TKKD variable is well distributed. PAD with a maximum of 46.75, minimum of 3.84, standard deviation of 9.47, and mean of 14.02 proves that the PAD variable is well distributed. BP with a maximum of 39.90, minimum of 16.25, standard deviation of 5.85, and mean of 32.30 proves that the TKKD variable is well distributed. BM with a maximum of 26.75, a minimum of 9.55, a standard deviation of 4.09, and a mean of 18.87 proves that the TKKD variable is well distributed with a total of 65 data.

Multiple linear regression

Table 3 presents the results of the multiple regression analysis of the research equation model.

Table 3. Multiple Linear Regression (REM)

—	Variable	Coefficient	Std. Error	t-Statistic	Prob.
	C	0.738287	3.865917	0.190973	0.8492
	PAD	2.090045	0.055532	37.63661	0.0000
	BM	0.126010	0.091019	1.384438	0.1713
	BP	-0.439492	0.092006	-4.776799	0.0000

Source: Results from Eviews 12, 2023

Based on the table above, the following regression equation is obtained :

$$TKKD = 0.74 + 2.09PAD - 0.44BP + 0.13BM$$

The interpretation of the multiple linear regression test equation is as follows:

1. Based on Table 3, it shows a constant value of 0.74. It can be understood that the independent variable is 0 or nil, so the dependent variable has increased by 0.74.
2. The value of the coefficient of the regional original income (PAD) variable shows the number 2.09, which means that if employee spending increases by 1%, the level of regional financial independence will increase by 2.09.
3. The value of the coefficient for the employee expenditure variable (BP) is -0.44, which means that if employee expenditure increases by 1%, the level of regional financial independence will increase by -0.44.
4. The value of the capital expenditure (BM) variable coefficient shows 0.13, which means that if capital expenditure increases by 1%, the level of regional financial independence will decrease by 0.13.

Hypothesis Test Results

The test results of the influence of local revenue (PAD), capital expenditure (BM), and employee expenditure (BP) are explained in Table 4.

Table 4. Hypothesis Test Results

—	Variable	Coefficient	Std. Error	t-Statistic	Prob.
	C	0.738287	3.865917	0.190973	0.8492
	PAD	2.090045	0.055532	37.63661	0.0000
	BM	0.126010	0.091019	1.384438	0.1713
	BP	-0.439492	0.092006	-4.776799	0.0000

Source: Results from Eviews 12, 2023

It can be concluded regarding the hypothesis partially from each independent variable to the dependent variable. Based on the results of the hypothesis test, it can be seen that the probability value of PAD is $0.00 < 0.05$, so H_0 is rejected and H_1 is accepted. This means that regional original income influences the level of regional financial independence so the first hypothesis in this research is proven true. Capital expenditure (BM) with a probability value of $0.00 < 0.05$ then H_0 is rejected and H_2 is accepted. This means that employee spending influences the level of regional financial independence so the second hypothesis in this research is proven true. Meanwhile, employee expenditure (BP) has a probability value of $0.17 > 0.05$, so H_0 is accepted and H_3 is rejected. This means that capital expenditure has no effect on the level of regional financial independence, so the third hypothesis in this research is not proven true.

Coefficient of Determination

The results of the determination coefficient test for the variables Regional Original Income (PAD), Capital Expenditures (BM), and Employee Expenditures (BP) explain the level of regional financial independence described in Table 5.

Table 5. Coefficient of Determination (R²)

—			
Weighted Statistics			
R-squared	0.960323	Mean dependent var	6.462894
Adjusted R-squared	0.958372	S.D. dependent var	7.596348
S.E. of regression	1.549885	Sum squared resid	146.5308
F-statistic	492.1378	Durbin-Watson stat	1.637854
Prob(F-statistic)	0.000000		

Source: Results from Eviews 12, 2023

The results of data processing from the coefficient of determination test (R^2) in Table 5 above produce *R-Square* and *Adjusted R-Square values* of 0.96 or 96%. These results can be interpreted as meaning that the contribution level of the regional original income, personnel expenditure, and capital expenditure variables to the variable level of regional financial independence in this study is 96% and the remaining 4% is contributed by other variables outside the research variables.

Original regional income is not only a source of regional income, but also a benchmark that shows the performance of the regional government concerned in managing regional finances and economic development which can have an impact on the level of independence of a region (Sefira & Budiwitjaksono, 2022).

The results of this research are in line with research conducted by Angelina, et al (2020), Machmud, et al (2021), Kristina, et al (2021), Darmayanti, et al (2022), and Oktavianti, et al (2023) that regional original income has an effect on the level of regional financial independence, but this contradicts research from Kusmila (2023) and Adhim, et al (2023) that regional original income does not affect the level of regional financial independence.

Regional independence can be achieved if the government system runs well, one of which is the performance of regional officials. Personnel expenditure has a positive influence on regional independence, where the amount of personnel expenditure can encourage the productivity of regional officials' performance. However, this contradicts research conducted by Sefira and Budiwitjaksono (2022), Defitri (2020), and Fitriyani and Suwarno (2021) which stated that employee spending does not affect the level of regional financial independence.

Abdullah, Sari, and N. (2022) mean that when capital expenditure increases, this is meaningless or does not have a big impact on the level of regional financial independence. The government's hopes for the employees involved to improve their performance did not go well. One of the factors that causes this to happen is the lack of good capital expenditure management and the large number of public sectors that have not yet developed. The development of industrial infrastructure has a real impact on increasing PAD. In other words, the construction of these various facilities will lead to increased regional independence.

The results of this research are in line with research conducted by Andriana (2020), Affifah and Rahayu (2021), and Saraswati and Nurharjanti (2021) which stated that capital expenditure does not affect the level of regional financial independence. However, this research is not in line with research conducted by Abdullah, et al (2022), Angelina, et al

(2020), Riyadi (2022), and Oktavianti, et al (2023) which states that capital expenditure influences the level of regional financial independence.

Conclusion

From this discussion, it can be concluded that regional original income has an influence on the level of regional financial independence, personnel expenditure has an influence on the level of regional financial independence, and capital expenditure has no influence on the level of regional financial independence.

For this reason, the government in various regions in Eastern Indonesia is expected to be able to improve performance and evaluate both the performance and capabilities of regional resources and maximize capital expenditure by building connectivity between regions to increase PAD so that it can continue to operate well and improve the regional economy which will have an impact both at the level of regional financial independence.

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